EXTRACT FROM BY-LAWS

Section 9. No book shall, at any time, be taken from the Library Room to any other place than to some court room of a Court of Record, State or Federal, in the City of San Francisco, or to the Chambers of a Judge of such Court of Record, and then only upon the accountable receipt of some person entitled to the use of the Library. Every such book so taken from the Library, shall be returned on the same day, and in default of such return the party taking the same shall be suspended from all use and privileges of the Library until the return of the book or full compensation is made therefor to the satisfaction of the Trustees.

Sec. 11. No books shall have the leaves folded down, or be marked, dog-eared, or otherwise soiled, defaced or injured. Any party violating this provision, shall be liable to pay a sum not exceeding the value of the book, or to replace the volume by a new one, at the discretion of the Trustees or Executive Committee, and shall be liable to be suspended from all use of the Library till any order of the Trustees or Executive Committee in the premises shall be fully complied with to the satisfaction of such Trustees or Executive Committee.

NOS. 9781 AND 9782

Vol. I
2270

United States Circuit Court of Appeals

For the Ninth Circuit.

WILSON BROTHERS & COMPANY (Wilson Bros. & Co.), a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Transcript of the Record

Upon Petitions to Review Decisions of the United States Board of Tax Appeals

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

No. 9781

United States

Circuit Court of Appeals

For the Ninth Circuit.

WILSON BROTHERS AND COMPANY, (Wilson Bros. & Co.,) a corporation,

Petitioner,

vs.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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APPEARANCES

For Taxpayer:
A. E. GRAUPNER, Esq.

For Comm'r:
T. M. MATHER, Esq.,
ALVA C. BAIRD, Esq.

Docket No. 93668

WILSON BROTHERS & COMPANY, (WILSON BROS. AND CO.,) a corporation,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

1938

May 21—Petition received and filed. Taxpayer notified. (Fee paid).

May 21—Copy of petition served on General Counsel.

June 21—Answer filed by General Counsel.

June 21—Request for circuit hearing in San Francisco, California, filed by General Counsel.

June 25—Notice issued placing proceeding on San Francisco, California Calendar. Service of answer and request made.

1939

Mar. 25—Hearing set May 29, 1939, San Francisco, Calif.

June 6-7—Called 5-28-39. Hearing had before Mr. Disney on merits. Submitted, Motion to consolidate Dockets 83397 and 93668 granted. Stipulation as to the facts filed. Briefs due Aug. 1, 1939; Reply Sept. 1, 1939.

June 24—Transcript of hearing June 6, 1939 filed.

June 24—Transcript of hearing June 7, 1939 filed.

July 6—Motion for leave to file amended petition, amended petition lodged, filed by taxpayer. 7-10-39 granted. 7-11-39 copy served on General Counsel.

July 28—Brief filed by taxpayer.

July 31—Answer to amended petition filed by General Counsel.

Aug. 2—Copy of brief served on General Counsel.

Aug. 3—Copy of answer to amended petition served on taxpayer.

Aug. 29—Reply brief filed by taxpayer.

1940

May 22—Memorandum opinion rendered, Richard L. Disney, Div. 4. Decision will be entered under Rule 50.

June 17—Motion for review by the entire Board, or for reconsideration, filed by taxpayer.

June 20—Computation of deficiency filed by General Counsel.

June 28—Order denying petitioner's motion for reconsideration, entered.

1940

July 2—Order denying review by the Board, entered.

July 9—Hearing set July 31, 1940, on settlement. [1*]

July 22—Consent to settlement filed by taxpayer.

Aug. 6—Decision entered, R. L. Disney, Div. 4.

Oct. 31—Petition for review by United States Circuit Court of Appeals, Ninth Circuit, with assignments of error filed by taxpayer.

Oct. 31—Affidavit of service filed by taxpayer.

Nov. 1—Proof of service of petition for review filed.

Dec. 30—Certified copy of order from 9th circuit enlarging time to 2-3-41 to prepare and transmit record filed.

1941

Jan. 8—Statement of evidence filed by taxpayer.

Feb. 3—Certified copy of order from the 9th Circuit, extending the time to April 3, 1941, to prepare and transmit record, filed.

Mar. 11—Agreed revised statement of evidence filed.

Mar. 11—Statement of points on which petitioner intends to rely filed, with proof of service thereon.

Mar. 11—Agreed designation of contents of record filed, with proof of service thereon.

Mar. 14—Certified copy of an order from the 9th Circuit, consolidating Dockets 83397, 93668, filed. [2]

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*Page numbering appearing at foot of page of original certified Transcript of Record.

United States Board of Tax Appeals

Docket No. 93668

WILSON BROTHERS AND COMPANY (Wilson Bros. & Co.), a corporation, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

MOTION FOR ORDER GRANTING LEAVE TO FILE AMENDED PETITION

Now comes the petitioner above-named by its counsel, Adolphus E. Graupner and Louis D. Janin, and moves this Honorable Board to grant petitioner leave to file an amended petition in the above-entitled proceeding, which said amended petition is presented herewith for consideration on this motion.

The foregoing motion is made in order to have the pleadings accord with the proofs submitted at the hearing of this proceeding in San Francisco, California, on June 6th and 7th, 1939, and to comply with the provisions of Rule 6(e) of this Board.

Respectfully submitted,

ADOLPHUS E. GRAUPNER

LOUIS D. JANIN

Counsel for Petitioner.

Dated July 1, 1939.

Granted July 10, 1939.

(Signed) [Illegible]

Member U. S. Board of Tax Appeals.

[Endorsed]: U. S. B. T. A. Filed July 6, 1939.

[3]

[Title of Board and Cause.]

AMENDED PETITION

Upon consent of the above-entitled Board to amend the petition in the above-entitled proceeding to conform to the proofs submitted at the hearing thereof and without waiver of right to challenge the constitutionality of any part of any Revenue Act involved in this proceeding or any act of the Commissioner of Internal Revenue or his subordinates, or to object to the jurisdiction of this Board, the petitioner above named hereby petitions for a redetermination of the alleged deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (IT:Aj-RLT-25579-90D) dated March 8, 1938, and as a basis of this proceeding alleges as follows:

1. The petitioner is a corporation duly organized and existing under the laws of the State of Nevada, with its principal office at 1112 Russ Building in the City and County [4] of San Francisco, State of California.

2. The notice of deficiency upon which the petition is based (a copy of which is hereunto attached and marked Exhibit "A") was mailed to the petitioner on March 8, 1938.

3. The asserted deficiency in tax here in controversy is for alleged income taxes for the calendar year 1934, and, as asserted in said purported deficiency notice, in the amount of not more than $14,313.88 for said year, including surtax and penalty

for alleged negligence on the part of petitioner in the respective amounts of $11,017.81 and $681.61.

4. The determination or proposal of a deficiency as set forth in said notice of deficiency is erroneous in each and every one of the following particulars assigned as errors:

(a) The Commissioner erred in proposing, determining and asserting against petitioner any amount as a deficiency in income tax for the calendar year 1934.

(b) The Commissioner erred in concluding, determining and asserting that petitioner was for the taxable calendar year 1934, subject to the provisions of Section 102(a) of the Revenue Act of 1934, as a corporation formed or availed of for the purpose of preventing the imposition of the surtax or any other tax on its shareholders, or was in any way used to prevent imposition of tax upon any person.

(c) The Commissioner erred in failing to determine the proper adjusted basis for depreciation as of December 31, 1931, with respect to the steamships "Idaho" and "Oregon" and the furniture and fixtures belonging to petitioner and in using an erroneous alleged "cost" as such basis. [5]

(d) The Commissioner erred in disallowing the sum of $5,211.21 or any portion of the depreciation claimed by petitioner as a deduction from gross income for the taxable calender year 1934, and in not allowing at least $2,639.89 depreciation in addition to the amount claimed on the return.

(e) The Commissioner erred in disallowing the sum of $15,144.40 or any portion of the allowance or deduction for bad debts or losses claimed by petitioner as a deduction from gross income for the taxable calendar year 1934.

(f) The Commissioner erred in adding to petitioner's income, as returned for the taxable calendar year 1934, the amount of $25,057.00, or any portion thereof, representing dividends received by petitioner in said year from domestic corporations subject to tax under the provisions of the Revenue Act of 1934 and earlier Revenue Laws.

(g) The Commissioner erred in asserting, determining and attempting to impose on the petitioner in addition to the tax liability as returned by petitioner, as a penalty asserted for negligence as defined in Section 293(a) of the Revenue Act of 1934, the sum of $681.61 or any other amounts.

(h) The Commissioner erred in alleging, asserting and determining that petitioner received income in or was liable to tax for the calendar year 1934 in any amount greater than that as returned by petitioner for said year, and particularly in attempting to impose additions to petitioner's income and tax for said year under alleged authority of Sections 102(a) or 293(a) of the Revenue Act of 1934. [6]

5. The facts upon which petitioner relies as a basis for this proceeding are as follows:

(a) Petitioner is a corporation duly organized on December 14, 1928, under the laws of the State

of Nevada. Its correct name and title is "Wilson Bros. & Co." instead of "Wilson Brothers and Company", as stated in the notice of deficiency. Its sole stockholders are Francis A. Wilson and Winfred T. Wilson.

(b) Petitioner was formed to take over the business of a copartnership of the same name and to acquire, own and operate timber lands, saw mills, logging railroads and equipment, and steamships; also, to buy, sell and transport lumber, to own, operate and maintain steamships and to utilize the same for the transport of cargoes.

(c) During said taxable year, petitioner kept and maintained its books of account on the accrual basis.

(d) On or about March 15, 1935, petitioner filed its income tax return for the taxable calendar year 1934 in which it reported no taxable income for said year. Said return stated specifically the items of petitioner's gross income, the deductions and credits claimed by it.

(e) The Commissioner has erroneously and illegally proposed and determined against petitioner for the taxable year 1934 a deficiency in income tax in the amount of $2,614.46, an additional tax for said year in the amount of $13,632.27 by erroneous and illegal application of Section 102(a) of the Revenue Act of 1934, and penalties of five per cent on each of the amounts above mentioned by erroneous and illegal [7] application of Section

293(a) of the Revenue Act of 1934; or a total deficiency and penalty of $14,313.88.

(f) Respondent added to the amount of total income reported by petitioner in its income tax return for the taxable calendar year 1934 the amount of $5,211.21 designated in the deficiency notice as "Excessive depreciation". Petitioner had claimed as deductible depreciation in its return the following and only the following items and amounts with respect to assets used in the trade or business:

Wooden buildings	$ 500.00
Steamers "Idaho" and "Oregon"	8,750.00
Furniture and fixtures	500.00
Automobiles	1,649.85
Or a total of	$11,399.85

Respondent's disallowance of items of deduction in the deficiency notice in this proceeding has not been itemized or specifically explained therein, or in his answer to the original petition on file herein or by proofs at hearing of this proceeding.

(g) Petitioner has stipulated to the disallowance of depreciation claimed on wooden building in the amount of $500.00 which was the total amount claimed. Petitioner has also stipulated that the allowable depreciation on automobiles for the year 1934 is the amount of $1,163.66.

(h) The basis to petitioner for depreciation of its 75% interest in the steamship "Idaho", without allowance for depreciation in prior years, was on

December 31, 1931, at least $200,216.67; the depreciation claimed and allowed by respondent [8] to said date was $108,750.00, as has been stipulated; the petitioner's depreciable basis on said steamship as of December 31, 1931, as adjusted for depreciation allowed and allowable for prior years was at least $91,466.67.

(i) As determined in said deficiency notice said steamship "Idaho" had a useful depreciable life of not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date; and petitioner is and was entitled to an annual depreciation allowance of not less than $6,097.11 for said period.

(j) The basis to petitioner for depreciation on its 100% interest in the steamship "Oregon", without allowance for depreciation in prior years, was on December 31, 1931, at least $205,766.32; the depreciation claimed and allowed by respondent to said date was $109,231.69, as has been stipulated; the petitioner's depreciable basis on said steamship as of December 31, 1931, as adjusted for depreciation allowed and allowable for prior years was at least $96,434.63.

(k) As determined in said deficiency notice said steamship "Oregon" had a useful depreciable life not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date, and petitioner is and was entitled to an annual depreciation allowance of not less than $6,437.64 for said period.

(l) That on January 2, 1929, petitioner acquired furniture and fixtures of a fair market value of not less than $5,000.00, on which respondent has determined a useful and depreciable life of ten years. From January 2, 1929, respondent [9] has allowed $1,500.00 depreciation on said furniture and fixtures to December 31, 1931, and has determined a rate of 10% for depreciation on the remaining ten years of life thereof. Petitioner is therefore entitled to allowance for depreciation on said furniture and fixtures in an amount not less than $350.00 for the taxable year 1934.

(m) In its income tax return for the taxable calendar year 1934 petitioner sought deduction of the amount of $15,144.40 for bad debts which respondent has disallowed in the deficiency notice in this proceeding and added to petitioner's gross income for said year. Said deductions were for the following items:

Partial write off for depreciated value of Kentucky Fuel Gas Corporation Bonds	$5,500.00
Partial write off of indebtedness of Woodhead Lumber Co. of California	5,000.00
Partial write off of indebtedness of shareholders in the Steamship "Svea"	4,644.40

All of the foregoing items were written off in petitioner's books of account during the year 1934 after investigation of the real worth of said items made on behalf of petitioner and determination by it that

the amounts so written off were beyond hope of recovery and worthless, which was in fact the case.

(n) Petitioner is therefore entitled to deduct from its gross income of $63,901.60 as reported in its income tax return for the year 1934 and accepted by respondent in the deficiency notice upon which these proceedings were brought, the following [10] deductible items, viz:

Rent on business property, as accepted by respondent	$ 1,140.00
Taxes, as accepted by respondent	396.09
Loss on steamship operations, as accepted by respondent	2,173.18
Bad debts:	
Kentucky Fuel Gas Co.—partial write-off	5,500.00
Woodhead Lumber Co.—partial write-off	5,000.00
Steamship "Svea" expense, partial write-off	4,644.40
Dividends, as accepted by respondent	25,057.00
Depreciation:	
Steamship "Idaho", 75% interest, not less than	6,097.77
Steamship "Oregon", 100% interest, not less than	6,437.64
Furniture and Fixtures, not less than	350.00
Automobiles, as stipulated	1,163.66
Salaries and wages, accepted by respondent	5,815.00
General expense, accepted by respondent	4,117.44
or a total of	$67,892.18
and an excess over deductions claimed in the return of	2,649.22
with a resulting loss of	3,990.57

(o) Petitioner was not formed or availed of for the purpose of preventing the imposition of surtax upon its shareholders or the shareholders of

any other corporation through the medium of permitting gains and profits to accumulate instead of being divided or distributed.

(p) During the year 1934 the economic and financial depression which started in 1929 continued and the impaired and shrunken market value of the assets of petitioner made it in- [11] advisable under sound business practice to declare any dividends or in any other way further impair the assets of the corporation and thus endanger the accomplishment of the business purposes for which petitioner was organized.

(q) Under the facts of this proceeding petitioner is not liable for surtax under section 102 of the Revenue Act of 1934, in any amount upon any possible fair adjustment of its net income for the taxable calendar year 1934.

(r) Under the facts of this proceeding petitioner is not liable for the penalty of five per cent sought to be imposed by respondent under the alleged authority of section 293(a) of the Revenue Act of 1934, because the deficiency notice and the testimony adduced shows no negligence, or intentional disregard of rules and regulations, and respondent failed to offer proof in support of his attempt to impose such a penalty.

Wherefore, petitioner prays that this Board may hear the proceeding and grant to petitioner such relief from deficiency, additional tax and penalty

asserted by Commissioner as may be within the jurisdiction of the Board.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for Petitioner,
1110 Balfour Building,
San Francisco, California. [12]

State of California,
City and County of San Francisco—ss.

Francis A. Wilson, being duly sworn, says that he is the president of the above-named incorporated petitioner and that he is authorized to verify the foregoing petition; that he has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true, except as to those facts stated to be upon information and belief, and those facts he believes to be true.

FRANCIS A. WILSON (signed)

Subscribed and sworn to before me this 30th day of June, 1939.

HAZEL E. THOMPSON
Notary Public in and for the City and County of San Francisco, State of California.

My Commission Expires September 21, 1942. [13]

EXHIBIT "A"

TREASURY DEPARTMENT
Washington

Mar. 8, 1938

Office of
Commissioner of
Internal Revenue

Address Reply
to
Commissioner of
Internal Revenue

And Refer to

Wilson Brothers and Company,
1112 Russ Building,
San Francisco, California.

Sirs:

You are advised that the determination of your income tax liability for the taxable year(s) ended December 31, 1934 discloses a deficiency of $14,-313.88, income tax, surtax and penalties, as shown in the statement attached.

In accordance with section 272(a) of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C1:P:7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,
GUY T. HELVERING,
Commissioner.
By JOHN R. KIRK (signed)
Deputy Commissioner.

Enclosures:
Statement
Form 870 [14]

STATEMENT

Wilson Brothers and Company,
1112 Russ Building,
San Francisco, California

SUMMARY OF TAX LIABILITY

Income Tax Section 13

Taxable Year Ended	Tax Liability	Tax Assessed	Deficiency	5% Penalty
December 31, 1934	$ 2,614.46	None	$ 2,614.46	$ 130.7
Surtax, Section 102				
December 31, 1934	11,017.81	None	11,017.81	550.8
Total	13,632.27	None	13,632.27	681.6
Total Deficiencies and penalties				$14,313.8
Net loss reported on return				1,341.3
Add:				
1. Excessive depreciation			5,211.21	
2. Bad debts disallowed			15,144.40	20,355.6
Net income adjusted for income tax				$19,014.2

EXPLANATION OF ADJUSTMENTS

1. The excessive depreciation has been disallowed in accordance with section 23(1) of the Revenue Act of 1934 and Treasury Decision 4422, the computation of which is shown in exhibit (a) of the revenue agent's report, a copy of which was furnished you on April 12, 1937.

2. The bad debts have been disallowed in accordance with section 23(k) of the Revenue Act of 1934 for the reason no evidence has been submitted to

establish the worthlessness thereof and no permission has been granted you to change from the actual bad debt basis elected in prior years to the reserve basis. [15]

Computation of Income Tax, Section 13

Net income subject to 13¾% tax	$19,014.25
Income tax liability	2,614.46
Income tax assessed	None
Income tax deficiency	$ 2,614.46
5% penalty	130.72
Total income tax deficiency and penalty	$ 2,745.18

Computation of Surtax, Section 102

Net income adjusted for income tax	$19,014.25
Add:	
Dividends received	25,057.00
Net income adjusted subject to 25% surtax	$44,071.25
Surtax liability	$11,017.81
Surtax assessed	None
Surtax deficiency	$11,017.81
5% penalty	550.89
Total surtax deficiency and penalty	$11,568.70
Total income and surtax deficiencies and penalties	$14,313.88

An examination of the balance sheets submitted with the return leads the Bureau to conclude that your corporation is an investment corporation and subject to the provisions of section 102 of the Revenue Act of 1934.

The understatement of tax for the year 1934 is attributable to negligence and in accordance with the provisions of section 293(a) of the Revenue Act of 1934 a penalty of 5 percent of the deficiencies attached. [16]

The interest due on the deficiencies as provided by law will be computed by this office and demanded by the collector of internal revenue at the time you are called upon to pay the tax.

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him.

[Endorsed]: U. S. B. T. A. Filed July 10, 1939. [17]

[Title of Board and Cause.]

ANSWER TO AMENDED PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the amended petition filed by the above-named petitioner, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the amended petition.

2. Admits the allegations contained in paragraph 2 of the amended petition.

3. Admits the allegations contained in paragraph 3 of the amended petition.

4. (a) to (h), inclusive. Denies the Commissioner erred in the determination of the deficiency as alleged in subparagraphs (a) to (h), inclusive, of paragraph 4 of the amended petition. [18]

5. (a) Admits the allegations contained in subparagraph (a) of paragraph 5 of the amended petition.

(b) Denies the allegations contained in subparagraph (b) of paragraph 5 of the amended petition.

(c) Admits the allegations contained in subparagraph (c) of paragraph 5 of the amended petition.

(d) Admits on or about March 15, 1935, petitioner filed its income tax return for the taxable calendar year 1934 in which it reported no taxable income for said year, as alleged in subparagraph (d) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(e) Denies the allegations contained in subparagraph (e) of paragraph 5 of the amended petition.

(f) Admits respondent added to the amount of total income reported by petitioner in its income tax return for the taxable calendar year 1934 the amount of $5,211.21 designated in the deficiency notice as "Excessive depreciation" as alleged in subparagraph (f) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(g) Admits the allegations contained in subparagraph (g) of paragraph 5 of the amended petition.

(h) Admits the depreciation allowed by respond-

ent was $108,750.00 as stipulated, as alleged in subparagraph (h) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph. [19]

(i) Admits, as determined in said deficiency notice said steamship "Idaho" had a useful depreciable life of not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date, as alleged in subparagraph (i) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(j) Admits the depreciation allowed by respondent was $109,231.69 as stipulated, as alleged in subparagraph (j) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(k) Admits, as determined in said deficiency notice said steamship "Oregon" had a useful depreciable life not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date, as alleged in subparagraph (k) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(l) Denies the allegations contained in subparagraph (l) of paragraph 5 of the amended petition.

(m) Admits in its income tax return for the taxable calendar year 1934 petitioner sought deduction of the amount of $15,144.40 for bad debts which respondent has disallowed in the deficiency notice

in this proceeding and added to petitioner's gross income for said year, as alleged in subparagraph (m) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph. [20]

(n), (o), (p), (q), (r). Denies the allegations contained in subparagraphs (n), (o), (p), (q) and (r) of paragraph 5 of the amended petition.

6. Denies generally and specifically each and every allegation in the amended petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and that the petitioner's appeal be denied.

(Signed) J. P. WENCHEL
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:
ALVA C. BAIRD,
T. M. MATHER,
Special Attorneys,
Bureau of Internal Revenue.

TMM:emb 7-22-39

[Endorsed]: U. S. B. T. A. Filed July 31, 1939.

[21]

United States Board of Tax Appeals

Docket No. 83397,
Docket No. 93667.

WILSON BROTHERS AND COMPANY, (Wilson Bros. & Co.), a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STIPULATION OF FACTS

It is hereby stipulated by and between the above-named parties hereto, through their respective counsel that the statements hereinafter contained may be considered as true, without prejudice of the right of either party to introduce other and further evidence not inconsistent herewith.

1. The two above numbered proceedings may be heard together and the facts herein stipulated and all material evidence and testimony introduced at such hearing may be considered by the Board of Tax Appeals in making its findings of fact and decisions in both or each of the above-numbered proceedings. [22]

2. The taxable years involved in Docket No. 83397 are 1932 and 1933 and the taxable year involved in Docket No. 93667 is 1934.

3. Prior to the organization of petitioner and on January 31, 1927, F. A. Wilson and W. T. Wilson formed a co-partnership under the name of Wilson

Bros. & Co., which co-partnership continued to do business under that name until after the formation of petitioner corporation under the same name, when said co-partnership was dissolved in January, 1929.

4. Wilson Bros. & Co. is a corporation duly organized and existing under the laws of the State of Nevada, with its principal office, during the taxable years involved, at room 1112 Russ Building, San Francisco, California.

5. On December 14, 1928, said F. A. Wilson and W. T. Wilson caused the incorporation of petitioner with a capital stock of 200,000 shares of a par value of twenty-five dollars per share to take over and continue the business of said co-partnership.

6. On December 31, 1918, each of said F. A. Wilson and W. T. Wilson purchased twenty shares of such capital stock (or a total of forty shares) and each paid to petitioner for said shares so purchased the amount of $500.00, or a total of $1,000.00.

7. No other shares of the petitioner corporation have ever been issued by it.

8. For the taxable years involved, petitioner filed income tax returns with the Collector of Internal Revenue, First District of California, as follows: [23]

For the taxable year 1932.....March 31, 1933,
For the taxable year 1933.....March 15, 1934,
For the taxable year 1934.....March 15, 1935.

9. By waivers the time for mailing notice of deficiency for the taxable year 1932 was extended to December 31, 1935, and notice of deficiency for that year was timely mailed.

10. The depreciation on wooden buildings as computed and disclosed in the statement attached to the deficiency notice for the taxable years 1932 and 1933 and as disallowed in the deficiency notice for the taxable year 1934 is accepted as being correct.

11. The amounts of depreciation deducted to December 31, 1931, on the shares or interests acquired by petitioner on January 2, 1929, in the steamships "Idaho" and "Oregon" as computed and allowed in the statement attached to the deficiency notice for the taxable years 1932 and 1933 are as follows:

Steamship "Idaho" $108,750.00
Steamship "Oregon" $109,231.69

12. The values, life and depreciation allowances of automobiles as set forth in the schedule attached to the report of the Revenue Agent for the year 1934, dated April 12, 1937, and which have been adopted and applied in the deficiency notices for each of the years herein involved are hereby accepted as correct, as follows:

Acquired	Cost	Depreciation to 12/31/31	Balance	Remaining Life	Depreciation Allowable per annum
1929 Lincoln	$5,498.75	$4,648.75	$850.00	2 years	$425.00
1930 Ford	652.50		652.50	3 years	214.16
1932 Studebaker	2,098.00			4 years	$524.50

13. The history of the Steamship "Idaho" to the time it was acquired by petitioner on January 2, 1929, is as follows:

The wooden hull of the vessel was built at Aberdeen, Washington, and completed about December 14, 1916. The vessel was constructed on order of and contract with Henry Wilson, for a sixty-five one-hundredths share, Charles R. Wilson Estate, Inc., a twenty-five one-hundredths share and A. B. Johnson a ten one-hundredths share. The completed cost of the vessel was to be and was $200,000.00

On December 14, 1916, the vessel was given temporary enrollment as a barge and was thereafter towed to Oakland, California, for installation of engines, machinery, and rigging. On or about February 6, 1917, the vessel was completed and Henry Wilson gave to his wife Mary H. Wilson, a twenty one-hundredths share in the vessel, to Winfred T. Wilson, his son, a five one-hundredths share and to Francis A. Wilson, his son, a five one-hundredths share. On February 6, 1917, a permanent enrollment certificate was granted by the Bureau of Navigation, in which the gross tonnage was stated as 1047 tons and the net tonnage as 558 tons. The names of the then owners were therein stated as

Henry Wilson	35/100ths
Mary H. Wilson	20/100ths
F. A. Wilson	5/100ths
W. T. Wilson	5/100ths
Others	35/100ths

On June 6, 1924, Henry Wilson executed a bill of sale with respect to his remaining interest of thirty-five [25] one-hundredths in favor of Mary H. Wilson, his wife. Said bill of sale stated a nominal consideration and was filed for record with the Department of Commerce, Bureau of Navigation on June 7, 1928. A copy of said bill of sale is attached hereto and marked Exhibit "A".

On July 17, 1925, A. B. Johnson and Mariett Johnson, his wife, executed a bill of sale to F. A. Wilson, covering their ten one-hundredths interest in the "Idaho". This transaction was evidenced by bill of sale stating a nominal consideration, dated July 17, 1925 and recorded July 20, 1935.

On July 21, 1925, F. A. Wilson transferred to W. T. Wilson, a five one-hundredths interest in said vessel by bill of sale stating a nominal consideration, dated July 21, 1925, and recorded on the same day.

On January 2, 1929, said Mary H. Wilson, W. T. Wilson and F. A. Wilson conveyed all of their interests, or a total of seventy-five one-hundredths shares in the steamship "Idaho" to petitioner. The instrument of transfer stated a nominal consideration and was recorded on June 3, 1929.

The dead weight tonnage of said "Idaho" was determined in 1918 by the United States Shipping Board to be 1834 tons.

14. The history of the steamship "Oregon" to the time it was acquired by petitioner on January 2, 1929, is as follows:

The wooden hull of the vessel was built in Aberdeen, Washington, and completed on August 9, 1916. The vessel was [26] constructed on order of and contract with Henry Wilson, for fifteen thirty-seconds, Charles R. Wilson Estate, Inc. for fifteen thirty-seconds, and A. B. Johnson, for two thirty-seconds shares. The completed cost of the vessel was to be and was $140,386.15.

On August 9, 1916, the vessel was given temporary enrollment as a barge and was thereafter towed to Oakland, California, for installation of engines, machinery and rigging. On or about October 25, 1916, the vessel was completed and a permanent enrollment certificate was granted by the Bureau of Navigation, in which the gross tonnage was stated as 989 tons and the net tonnage as 628 tons. The names of the then owners were stated therein as:

Henry T. Wilson	15/32nds
A. B. Johnson	2/32nds
C. R. Wilson Estate, Inc.	15/32nds

On December 4, 1918, Henry Wilson executed two bills of sale, each covering a 5/32nds interest in the SS "Oregon", one bill of sale named his son, Winfred T. Wilson as grantee, and the other named his son, Francis A. Wilson, as grantee, instruments were recorded on March 21, 1919.

On November 22, 1918, a certificate of partial ownership was recorded showing the distribution on liquidation of the C. R. Wilson Estate, Inc. of fifteen thirty-seconds interest in the "Oregon" to

Margaret A. Wilson, as trustee, for herself and her children, who were the heirs of Charles R. Wilson, deceased, and the stockholders of the C. R. Wilson Estate, Inc.

On September 30, 1919, Margaret A. Wilson, as trustee as aforesaid, conveyed the interests in the "Oregon" formerly held by the C. R. Wilson Estate, Inc. as follows:

To Henry T. Wilson.....5/32nds
To F. A. Wilson.....5/32nds, and
To W. T. Wilson.....5/32nds.

[27]

The bills of sale were recorded December 4, 1919, and the transfer was made upon a consideration based on a valuation of $125,000.00 for the entire vessel, or at a cost of $19,531.25 to each of the above named vendees.

On June 6, 1924, Henry Wilson executed a bill of sale with respect to a ten thirty-seconds interest in the "Oregon" in favor of Mary H. Wilson his wife. Said instrument stated a nominal consideration and was acknowledged on that date and filed for record with the Department of Commerce, Bureau of Navigation on June 7, 1928. A copy of said bill of sale is attached hereto and marked Exhibit "B".

On July 17, 1925, F. A. Wilson purchased from A. B. Johnson a two thirty-seconds share in the "Oregon". The bill of sale therefore was executed July 17, 1925, and recorded July 20, 1925.

On July 21, 1925 F. A. Wilson conveyed a one thirty-seconds share in the "Oregon" to his brother, W. T. Wilson, and the bill of sale, stating a nominal consideration, was recorded on the same day.

On January 2, 1929, said Mary H. Wilson, F. A. Wilson and W. T. Wilson transferred their entire interests, or a total of thirty-two thirty-seconds in the steamship "Oregon" to petitioner. The instrument of transfer, stated a nominal consideration and was recorded on July 3, 1929.

The dead weight tonnage of the said "Oregon" was determined in May, 1918 by the United States Shipping Board to be 1803 tons.

15. Throughout the years 1932, 1933 and 1934 [28] the ownership of petitioner in said steamships continued respectively as follows:

Steamship "Idaho" ..... 75% interest
Steamship "Oregon" .....100% interest

Witness our hands this 5th day of June, 1939.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Counsel for Petitioner
J. P. WENCHEL
Mather
Chief Counsel,
Bureau of Internal Revenue,
Counsel for Respondent.

[Endorsed]: U. S. B. T. A. Filed June 6, 1939. [29]

[Title of Board and Cause.]

Docket Nos. 83397, 93668.

Adolphus E. Graupner, Esq., and Louis D. Janin, Esq., for the petitioner.

Alva C. Baird, Esq., and T. M. Mather, Esq., for the respondent.

MEMORANDUM OPINION.

Disney: These proceedings are for a redetermination of deficiencies in normal income taxes, surtaxes and negligence penalties, as follows:

Docket No.	Year	Normal Tax	Additional Tax under section 104, 1932 Act (Under section 102, 1934 Act)	Penalty	Total
83397	1932	$ 477.61	$10,865.75	$ 567.17	$11,910.53
83397	1933	2,870.25	19,207.76	1,103.90	23,181.91
93668	1934	2,614.46	11,017.81	681.61	14,313.88

Pursuant to stipulation the two proceedings were heard together and are therefore consolidated for rendition of opinion. [30]

A stipulation of a part of the facts was filed. The facts stipulated are adopted by reference as a part of our findings of fact and, so far as deemed necessary to a determination of the issues involved, are, literally or in substance, set forth herein, together with other material facts found by us. Amended petitions and answers were filed in both proceedings.

The issues are excessive depreciation of properties, mainly those of depreciation of the steamers "Idaho" and "Oregon," and furniture and fixtures for the three years involved, the expense of maintenance of the steamships for the years 1932 and 1933, a question of interest for the years 1932 and 1933, the surtax for all of the years, partial write-off of bad debts as set up for 1933 and 1934, and a 5 per cent negligence penalty.

The particular items and amounts at issue allocated to each of the years involved are as follows:

	1932	1933	1934
1. Additional income asserted			
Alleged additional interest	$5,442.32	$ 445.18	None
2. Maintenance of steamships			
Disallowed as "Steamship operations"	4,547.05	4,412.26	Allowed
3. Partially Bad Debts Written Off			
(a) Woodhead Lumber Co., Acct's. rec.	None	None	$5,000.00
(b) SS "Svea", Acct. Rec.	None	2,160.80	4,644.40
(c) Kentucky Fuel Gas Corp. (bonds)	None	None	5,500.00
4. Additional depreciation allowable			
(a) Steamship "Idaho"	3,865.66	3,865.66	3,865.66
(b) Steamship "Oregon"	5,487.24	5,487.24	5,487.24
(c) Furniture and fixtures	151.98	151.98	151.98

5. Additional Tax alleged to be due under section 104 of the Revenue Act of 1932 and section 102 of the Revenue Act of 1934.

6. Negligence Penalty of 5 per cent alleged to be due under the provisions of section 293(a) of the Revenue Acts of 1932 and 1934.

[31]

On January 31, 1927, F. A. Wilson and W. T. Wilson formed a copartnership under the name of Wilson Bros. & Co., which copartnership continued

to do business under that name until after the formation of petitioner corporation under the same name, when said copartnership was dissolved in January 1929.

The petitioner is a corporation organized under the laws of Nevada with an authorized capital stock of 200,000 shares of a par value of $25 each, and with its principal office at 1112 Russ Building, San Francisco, California. It was organized on December 14, 1928, by F. A. Wilson and W. T. Wilson, to take over and continue the business of the partnership. On December 31, 1928, F. A. Wilson and W. T. Wilson each purchased 20 shares of stock and each paid to the petitioner therefor $500. No other shares have ever been issued. Petitioner during the taxable years kept its books upon the accrual system of accounting and filed income tax returns with the Collector for the First District of California.

Certain issues as to depreciation upon wooden buildings and automobiles have been settled by stipulation which will be reflected in decision under Rule 50. The other issues will be considered in the order above set forth, the facts, except the general facts as to incorporation stated above, being set forth separately in connection with discussion of each issue.

I. The first issue is with respect to additional income from interest, asserted in deficiency notices by respondent in amounts of $5,442.32 for the year 1932 and $445.18 for the year 1933. Those amounts

were, as [32] interest on bank deposits, added by the Commissioner to the respective amounts of $12,-949.58 and $9,035.81 reported by the petitioner, derived from bonds, accounts receivable and banks.

The respondent did not specify any particular sums upon which the alleged additional interest was accrued or paid to petitioner, but simply increased interest accrued or received in the amounts above stated. The petitioner adduced direct and positive testimony that it kept a monthly record of total interest received and that all interest accrued or paid to it during the years 1932 and 1933 from every source was included by it in its income tax returns, for the respective taxable years. It failed, however, to show all specific amounts of interest accrued or paid to it on the respective items, bank deposits, etc., during the taxable years, 1932 and 1933, now in issue, to produce the monthly accounts or to explain fully as to interest on a bank deposit of approximately $480,000.

Had the petitioner shown the specific amount of interest accrued or paid it on particular items, bank deposits and other items drawing interest, its evidence touching the same would be more satisfactory. However, a certified public accountant testified for the petitioner to the effect that he had verified and compared and ledgers of the banks and of the petitioner, and that all interest shown on the bank ledgers appeared on the books of the corporation, and that he could not find the interest items of $5,442.32 for 1932 and $445.18 for 1933 which the

respondent had added to petitioner's income. The deficiency notices mention only interest on bank deposits. In view of the direct and positive testimony [33] touching the subject, to the effect that the corporation kept an interest account of total interest received each month, and that ALL interest accrued or paid to it from ALL sources was duly reported and included in its income tax returns and the books of the corporation and the bank ledgers agreed, though the monthly records were not introduced, we are of the opinion, find and hold that the presumption of the correctness of the respondent's determination on this issue is overcome. Since petitioner reported approximately $13,000 interest for 1932 and about $9,000 for 1933, the interest on the $480,000 deposit is reasonably explained. We find and hold that with respect to this issue the respondent erred in determining that petitioner was taxable in 1932 on $5,442.32 as additional interest and $445.18 as additional interest in 1933, and determine this issue in favor of the petitioner. [34]

II. This issue relates to the maintenance and upkeep of two steamers, Idaho and Oregon. The facts involved are simple: The steamers were acquired by the petitioner in January, 1929 principally for the purpose of transporting lumber. After acquisition they were operated only five or six months before they were "laid up," because business got so bad that they could not be operated at a profit. The country then was experiencing a depression which lasted several years. During the tax-

able years in issue the steamers were kept in a seaworthy condition, in order that petitioner might use them if opportunity was afforded to profitably resume lumber transportations. The ships were never abandoned, but always were in charge of some one to look after them. The ships were put in dry dock and their bottoms were painted to protect and preserve them. Watchmen were employed and paid to look after them and certain supplies were furnished. Repairs were made to maintain the ships in proper serviceable condition. Petitioner always expected to put the ships back into commission and reengage in the shipping of lumber when conditions became favorable and the vessels, though not actively in use, were considered a part of the operating assets of the petitioner.

Under conditions in 1934 similar to those in 1932 and 1933, petitioner made claim in its 1934 return under the head of "Steamship operations" for the amount of $2,173.18, which sum was allowed as a deduction by the respondent. In each of the three taxable years the amounts reported in the income tax returns under the head of "steamship operations" were for the maintenance and upkeep of the Idaho and Oregon.

In our opinion expenses upon the vessels while temporarily laid up because of business conditions are in no different category than expenses while the vessels are at sea. The vessels were not abandoned. The business [35] of operating vessels had not been abandoned. On the entire record as presented we

hold on this issue that the respondent erred in not allowing the claimed deductions for maintenance and upkeep of the two steamers, for the years 1932 and 1933, as ordinary and necessary expense of business.

III. Whether the Commissioner erred in disallowing deductions for certain allegedly partially worthless debts claimed for the years 1933 and 1934, and charged off on the direct write-off method, is the next issue for our determination. The facts may be briefly stated, in connection with each item:

(a) Woodhead Lumber Company.—On January 1, 1934, the petitioner had accounts receivable from the Woodhead Lumber Co. of California amounting to $43,276.06. In its return for 1934, petitioner took a deduction for bad debts in the amount of $15,144.40, all of which was disallowed by the Commissioner. The petitioner was on the actual charge-off method of deducting bad debts.

In 1934 petitioner caused an examination of the affairs of the Woodhead Lumber Co. of California and from disclosures resulting from such examination reached the conclusion in 1934 that there could be only a partial recovery on said accounts receivable and that $5,000 would be a reasonable amount to write off and take as a deduction for such alleged partial bad debt during the year 1934 and such was taken.

There were two companies bearing the name of "Woodhead Lumber Company," one of California and the other of Nevada. In 1932, the Woodhead

Lumber Co. of Nevada bought the inventory and assets of the Woodhead Lumber Co. of California and gave to the latter its note for $25,000 and as collateral $37,000 face value of its capital stock, both of which were turned over to the petitioner. [36]

One witness was of the opinion that the note and stock described were of little or no value, but no facts appear to bear out such a conclusion. After the acquisition of the California company by the Nevada company, the petitioner did business with the Nevada company and is still selling lumber to it. Upon consideration of the entire record we find and determine that the alleged worthless character of the debt from the Woodhead Lumber Co. of California has not been shown. We therefore find and hold that the Commissioner did not err in disallowing the $5,000 deduction claimed.

(b) SS Svea.—The next item is with respect to accounts receivable from the steamship "Svea," which were written off by petitioner in the amount of $2,160.80 in 1933 and the amount of $4,644.40 in 1934 and disallowed by the Commissioner.

On January 1, 1933, accounts receivable from the steamship Svea amounted to $9,081.78 and on January 1, 1934, they amounted to $10,804.01. These accounts arose as follows: The Svea was a boat owned by many small owners, among whom were W. T. Wilson owning 7/128ths and F. A. Wilson owning a 9/128ths interest. The petitioner through the taxable years, 1933 and 1934, owned no interest in the

Svea, but was the managing, disbursing and collection agent for the steamship. When the boat was in operation, petitioner got a commission on the freight, but when the boat was not in operation petitioner received nothing, though the owners would expect the petitioner to make necessary advances to keep the boat in condition to be placed in operation again. There was a moral obligation to do so. Petitioner could anticipate repayment only from earnings or recovery from the owners of the boat. In 1933 the petitioner consulted its attorney as to whether it could recover sums which had been paid or advanced by it to the Svea for [37] maintenance of the boat, and was told that it did not look like recovery could be made and suit would be foolish. Thereupon $2,160 was written off as a bad debt; $2,160 was 20 per cent of the total expenditure. In 1934 it did not look like the boat would be put in operation for some little time, the account was constantly growing larger, and petitioner wrote off $4,644.40 as a bad debt.

The above facts do not, in our opinion, prove a deductible partially worthless debt. It is at least doubtful whether there was any promise on the part of anyone to pay, for the sole witness referred to petitioner's moral obligation to make the advances. No contractual obligation is shown. In the absence of a maturity date, and with an apparent limitation upon collectibility in that it was to be from earnings of the boat, there was no ordinary right of a

creditor. Commissioner v. Schmoll Fils Associated, Inc., ... Fed. (2d) ..... (C. C. A., 2nd Cir., March 18, 1940). Assuming, however, a debt and a debtor, there is no showing that the debtors were unable to pay. Who they are is not shown, except that the two stockholders of petitioner owned a one-eighth interest in the boat. The boat itself is not shown to have been encumbered so that collection by sale was impossible. In fact, all that petitioner shows is that it did not look as if the boat would be put into operation for some little time, and that an attorney advised that it would be foolish to sue and it did not look like anything could be recovered. Such opinion seems directed to the nature of the obligation as moral rather than legal. If it was devoted to solvency of the owners, it does not constitute the showing of fact required as to the debtor's financial condition. We hold that no error is shown in the disallowance of the deduction for partially worthless debts. [38]

(c) Kentucky Fuel and Gas Corporation Bonds.—The petitioner insists that the Commissioner erred in not allowing as a deduction, a write-off as a partial bad debt of $5,500 in 1934, with respect to Kentucky Fuel and Gas Corporation bonds. In 1934 petitioner owned bonds of Kentucky Fuel and Gas Corporation. Investigation was made during the year, upon which $5,500 was written off as a partial bad debt and deducted in petitioner's return. The bonds were a first mortgage upon the property of the company, which was an operating

company with considerable assets. It went into receivership about 1931. The record does not show when or from whom the bonds were acquired, the cost, nor whether in 1934 there was basis for partial charge off which did not exist in 1933 or earlier. The market value of the bonds, as shown by bid prices, declined from $74 on January 1, 1930, to $5 on December 31, 1931, to $2 on December 31, 1933, and $4.50 on December 31, 1934. Obviously such a record does not show error on the part of the Commissioner in denying the deduction. We hold that there was no error.

IV. The next issue is as to the proper amount of depreciation allowable in each of the taxable years on (a) the steamship Idaho, (b) the steamship Oregon, and (c) furniture and fixtures. The additional depreciation allowable as contended for by petitioner is for the years and in the amounts heretofore set forth above.

On January 2, 1929, the petitioner acquired a 75/100ths interest in the Idaho, and the entire interest in the Oregon, after a history of the two ships and in a manner, as follows:

(a) The wooden hull of the Idaho was completed about December 14, 1916. The vessel was constructed on order and contract with Henry Wilson for a 55/100ths share, Charles R. Wilson Estate, Inc., a 25/100ths share, and A. B. Johnson a 10/100ths share. The completed cost of the vessel was to be and was $200,000. Its fair market value on February 6, 1917, was not less than [39]

$395,000. The vessel Idaho was completed about February 6, 1917, and Henry Wilson gave his wife, Mary H. Wilson, a 20/100ths share in the vessel, to his son, Winfred T. Wilson, a 5/100ths share, and to another son, Francis A. Wilson, a 5/100ths share. On February 6, 1917, a permanent enrollment certificate was granted by the Bureau of Navigation in which the gross tonnage was stated to be 1,047 tons and the net tonnage as 558 tons. The names of the then owners were therein stated as:

Henry Wilson	35/100ths
Mary H. Wilson	20/100ths
F. A. Wilson	5/100ths
W. T. Wilson	5/100ths
Others	35/100ths

On June 6, 1924, Henry Wilson executed a bill of sale with respect to his remaining interest of 35/100ths in the Idaho in favor of Mary H. Wilson, his wife. Said bill of sale stated a nominal consideration but was in fact a gift and was filed for record with the Department of Commerce, Bureau of Navigation, on June 7, 1928. On July 17, 1925, A. B. Johnson and Mariett Johnson, his wife, executed a bill of sale to F. A. Wilson, covering their 10/100ths interest in the Idaho. This transaction was evidenced by bill of sale, stating a nominal consideration, though in fact F. A. Wilson paid them $11,716.67. On July 21, 1925, F. A. Wilson, in consideration of one-half the above sum, trans-

ferred to W. T. Wilson a 5/100ths interest in said vessel by bill of sale which, however, stated a nominal consideration and was recorded on the same day. On January 2, 1929, said Mary H. Wilson, W. T. Wilson and F. A. Wilson conveyed all of their interests, or a total of 75/100ths shares, in the steamship Idaho to petitioner. The instrument of transfer stated a nominal consideration of $10 and was recorded on June 3, 1929, but no consideration was paid. The transfer was a contribution [40] to petitioner's capital from Mary H. Wilson, F. A. Wilson and W. T. Wilson. The dead weight tonnage of said Idaho was determined in 1918 by the United States Shipping Board to be 1,834 tons.

(b) The wooden hull of the Oregon was completed on August 9, 1916. The vessel was constructed on order of, and contract with, Henry Wilson for 15/32nds, Charles H. Wilson Estate, Inc., for 15/32nds, and A. B. Johnson for 2/32nds, shares. The completed cost of the vessel was to be and was $140,386.15. Its fair market value on January 10, 1918, and on December 4, 1918, was not less than $385,000. About October 25, 1916, the vessel was completed and a permanent enrollment certificate was granted by the Bureau of Navigation in which the gross tonnage was stated as 989 tons and the net tonnage as 628 tons. The names of the then owners were stated therein as:

Henry T. Wilson 15/32nds
A. B. Johnson 2/32nds
C. R. Wilson Estate, Inc. 15/32nds

On or about January 10, 1918, Henry Wilson and Mary H. Wilson, his wife, executed and delivered a deed of gift to W. T. Wilson and F. A. Wilson, each, to a 5/32nds interest in the various properties operated or held in the firm name of Wilson Bros. & Co., including real estate, securities, merchandise, machinery, vessels, etc. On December 4, 1918, Henry Wilson executed two bills of sale, each covering a 5/32nds interest in the steamship Oregon. One bill of sale named his son, W. T. Wilson, as grantee, and the other named his son, F. A. Wilson, as grantee. The instruments were recorded on March 21, 1919, and were confirmatory of the gifts of January 10, 1918. On November 22, 1918, a certificate of partial ownership was recorded showing the distribution on liquidation of the C. R. Wilson Estate, Inc., of 15/32nds interest in the Oregon to Margaret A. Wilson, as trustee, for herself and her [41] children, who were the heirs of Charles R. Wilson, deceased, and the stockholders of the C. R. Wilson Estate, Inc.

On September 30, 1919, Margaret A. Wilson, as trustee as aforesaid, conveyed the interests in the Oregon formerly held by the C. R. Wilson Estate, Inc., as follows:

To Henry T. Wilson 5/32nds
To F. A. Wilson .....5/32nds, and
To W. T. Wilson .....5/32nds.

The bills of sale were recorded December 4, 1919, and the transfer was made upon a consideration

based on a valuation of $125,000 for the entire vessel, or at a cost of $19,531.25 to each of the above named vendees. On June 6, 1924, Henry Wilson executed a bill of sale with respect to a 10/32nds interest in the Oregon (a gift) in favor of Mary H. Wilson, his wife. Said instrument stated a nominal consideration and was acknowledged on that date and filed for record with the Department of Commerce, Bureau of Navigation, on June 7, 1928. On July 17, 1925, F. A. Wilson purchased from A. B. Johnson a 2/32nds share in the Oregon. The bill of sale therefor was executed July 17, 1925, and recorded July 20, 1925. The consideration paid was $4,954.72. On July 21, 1925, F. A. Wilson for and in consideration of one half of said amount conveyed a 1/32nd share in the Oregon to his brother, W. T. Wilson, and the bill of sale, stating a nominal consideration, was recorded on the same day. Thereafter, F. A. Wilson and W. T. Wilson each owned 11/32nds interest in the Oregon and their mother, Mary H. Wilson, owned 10/32nds interest therein. On January 2, 1929, said Mary H. Wilson, F. A. Wilson and W. T. Wilson transferred their entire interests, or a total of 32/32nds, in the steamship Oregon to petitioner, the transfers being a [42] contribution without consideration, though the instrument of transfer stated a nominal consideration and was recorded on July 3, 1929. The dead weight tonnage of the Oregon was determined in May 1918 by the United States Shipping Board to be 1,803 tons.

Throughout the years 1932, 1933 and 1934 the ownership of petitioner in said steamships continued respectively as follows:

Steamship "Idaho"	75% interest
Steamship "Oregon"	100% interest

The dispute between the parties on this issue is due to the difference in the basis selected to be used for depreciation. The amounts of depreciation deducted to December 31, 1931, on the shares or interests acquired by petitioner on January 2, 1929, in the steamships Idaho and Oregon as computed and allowed in the statement attached to the deficiency notice for the taxable years 1932 and 1933 are as follows:

Steamship "Idaho"	$108,750.00
Steamship "Oregon"	109,231.69

The petitioner accepts the totals of depreciation allowable and allowed to December 31, 1931, accepts 15 years as the extended life of the depreciable items and 6-2/3 per cent as the proper rate of depreciation, all as determined by the respondent in the deficiency notices, but insists the respondent adopted an incorrect basis for depreciation as of January 1, 1932, resulting in error in the amount of depreciation allowable thereon for the three taxable years, 1932, 1933 and 1934; also that in fixing a basis for depreciation on the two vessels the respondent relied upon the original cost of the steamships and did not take into consideration the fact that the interests owned by the petitioner on Jan-

uary 2, 1929, came into possession of the donors thereof in fractional shares acquired at different times and [43] under different circumstances. Petitioner's position is therefore that the total of the bases of the shares, with allowance for depreciation only for the period such shares were held by petitioner's donors, constitutes the basis of depreciable value for each ship. The parties seem in agreement upon the proposition that the basis for depreciation is cost, the fair market value on date of any gift, made prior to January 1, 1921, and as to acquisitions by gift made after December 31, 1920, cost or other basis in the hands of the donor or the last preceding owner by whom it was not acquired by gift. Section 114 (a) and 113 (a) (2), (4), Revenue Act of 1932.

The respondent now contends as to the 75 per cent interest owned by the petitioner in the Idaho that 10 per cent was purchased July 17, 1925, at a cost of $11,716.67, that 30 per cent was acquired by gift February 6, 1917, of a value of $131,666.66, and that 35 per cent was acquired by gift on June 6, 1924, but that no basis is shown. He therefore calculates a total base of $143,383.33, and, it being agreed that $108,750 had already been allowed as depreciation prior to January 1, 1932, contends for a residual base of $34,633.33. The petitioner agrees that the 10 per cent interest cost $11,716.67 on purchase on July 17, 1925, but contends that the 30 per cent interest acquired February 6, 1917, had a value of $118,500, being 30 per cent of a total value for

the Idaho of $395,000; also that the gift of a 35 per cent interest made July 6, 1924, had a base of $70,000, based on a construction cost of $200,000. It thus appears that we must decide (a) the value of the boat on February 6, 1917, and (b) what basis, if any, is proved for the gift of a 35 per cent interest on June 6, 1924. The evidence establishes, and we find, that the Idaho had a total value of $395,000 on February 6, 1917. The evidence is, and we find, that in 1917 the fair [44] market value of a fractional interest in a boat was its proportionate part of the total value. Therefore the 10 per cent interest which passed without consideration other than stock to the corporation in January 1929 from its two stockholders, W. T. Wilson and F. A. Wilson, would have a basis of $39,500, since under section 113 (a) (8) (B), Revenue Acts of 1932 and 1934, such contribution to the corporation takes a basis the same as in their hands, and they having acquired it by gift from their father prior to January 1, 1921, in their hands the base was the fair market value at time of acquisition by them. Section 113 (a) (4), Revenue Acts of 1932 and 1934. Likewise the other 10 per cent contributed to the corporation by the two stockholders and acquired by them by purchase in 1925 takes a basis of cost to them, i. e., $11,716.67. As to the basis for the gift of a 35 per cent interest made June 6, 1924: The total cost of construction of the Idaho was $200,000. Was the cost to Henry Wilson, donor on June 6, 1924, proportionate thereto? The respondent con-

tends that cost to Henry Wilson has not been shown. On the deficiency notice introduced in evidence in general, with respondent's counsel stating that he has no objection, it appears that the respondent in computing the depreciation used $200,000 as "cost," 75 per cent as "Interest owned by Wilsons" and "cost of interest" as $150,000. It is stipulated that the vessel was constructed on order of and contract with Henry Wilson for a "fifty-five one hundredths share." We think that the evidence clearly indicates that his base for 55 per cent would be 55 per cent of $200,000, or $110,000. He gave away 30 per cent on February 6, 1917, leaving only 25 per cent of the 55 per cent. Where [45] did he acquire the other 10 per cent which on February 6, 1917, he is recorded as owning on the permanent enrollment certificate issued by the Bureau of Navigation? Is the stipulation as to 55 per cent being constructed on his order a mistake intended to read "65%" or did he, between the time of construction of the ship and prior to February 6, 1917, acquire it in some other manner? The record is in fact silent, and therefore no base is clearly shown as to 10 per cent donated to his wife on June 6, 1924. We are inclined to believe that "65%" was intended, for the reason that the stipulation recites that the vessel was constructed 55 per cent on order of Henry Wilson, 25 per cent on order of Charles R. Wilson Estate, Inc., and 10 per cent on order of A. B. Johnson, thus totalling only 90 per cent. The construction of the hull was completed December 14, 1916.

Within 60 days, i. e., on February 6, 1917, Henry Wilson owned the missing 10 per cent, for he is recorded as owning 35 per cent after gifts of 30 per cent to his wife and sons. Moreover, as above set forth, the respondent in determining the deficiency gave the entire 75 per cent eventually acquired by petitioner a basis of cost of $200,000 total and $150,000 for the 75 per cent. Section 113 (a) (2) of the Revenue Act of 1932 provides as to basis of gifts after December 31, 1920:

> * * * If the facts necessary to determine such basis are unknown to the donee, the Commissioner shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. If the Commissioner finds [46] it impossible to obtain such facts, the basis shall be the fair market value of such property as found by the Commissioner as of the date or approximate date at which, according to the best information that the Commissioner is able to obtain, such property was acquired by such donor or last preceding owner.

We therefore conclude and hold that the basis of the entire 65 per cent donated on June 6, 1924, was cost, $130,000. Of the 65 per cent, 20 per cent passed by gift to Mary H. Wilson in 1917 and 35 per cent in 1924, and from her to the petitioner corporation in 1929. Since she was not a stockholder, this constituted a gift and under section 113 (a) (2) of the Revenue Acts of 1932 and 1934, the basis is that of the last preceding owner by whom the prop-

erty was not acquired by gift. The basis, therefore, of the 55 per cent is the cost to Henry Wilson, donor to Mary, or $110,000, being 55 per cent of the $200,000 cost of construction of the boat. Thus the total basis for the 75 per cent interest acquired by petitioner is $162,216.67. Subtracting therefrom $108,750 deducted to December 31, 1931, leaves $53,-466.67, the unadjusted basis for depreciation on December 31, 1931.

Petitioner argues that this should be adjusted by the subtraction of such portion of the $108,750 as was allowed as depreciation prior to acquisition of the 10 per cent interest by purchase on July 17 and 21, 1925, by the Wilson brothers. The necessary facts so to do are not in the record. The record shows the total depreciation $108,750 and petitioner urges us to prorate it over the years between construction of the boat and December 31, 1931. But the deficiency notice, above referred to, shows that the rate was not uniform throughout [47] the years. How many times it may have changed and therefore how much depreciation was in fact allowed to A. B. Johnson prior to his sale of the interest on July 17, 1925, the record does not show. We therefore hold that the basis for depreciation on December 31, 1931, as to the 75 per cent interest in the Idaho was $53,466.67.

(b) As to depreciation on the Oregon the parties agree on most of the items of basis in the sum of $164,429.22, but disagree as to the basis for gifts made after December 31, 1920, that is, a gift of

10/32nds interest on June 6, 1924, from Henry Wilson to his wife, Mary H. Wilson. We find that 5/32nds thereof was acquired by purchase from Margaret Wilson, Trustee, at a cost of $19,531.25 and that 5/32nds was acquired at cost of construction, i. e., 5/32nds of $140,386.15, or $21,935.35, and therefore conclude and hold that the total basis for depreciation to petitioner is therefore $205,796.32. Depreciation allowed prior to January 1, 1932, was $109,231.69, leaving $96,564.63 as unadjusted basis of depreciation on that date. Petitioner, as in case of the Idaho above discussed, urges adjustment to eliminate the depreciation allowed prior to purchase of interests donated to the petitioner. For the same reasons above set forth as to the Idaho, the lack of facts in the record, with which to make the desired adjustment, we hold that the basis for depreciation as to the Oregon on December 31, 1931, was $96,564.63.

(c) The furniture and fixtures of petitioner were taken over from its predecessor January 2, 1929, at a valuation of $5,000 and were so set up as an asset on its books of account. Petitioner in its returns began to depreciate said items on the basis of such value for a ten-year life and took deductions for depreciation thereon in its income tax returns for the years 1929, 1930 and 1931, in the amount of $500 per annum, or a 10 per cent rate [48] of depreciation, which for the said three years were allowed by the respondent. The record does not show when the furniture and fixtures were ac-

quired by the partnership (petitioner's predecessor) though they were taken over by the petitioner in January 1929 at a valuation of $5,000.

After recognizing for three years the $5,000 valuation and allowing a deduction for depreciation at a 10 per cent rate—$500 per year—the respondent determined that the furniture and fixtures instead of costing and having a value of $5,000, at which figure they were taken over by petitioner, cost the partnership and had a value of only $3,480.20 and after allowing the $1,500 depreciation for three years previously taken by the petitioner, found the residual cost and value to be only $1,980.20, upon which he allowed an annual 10 per cent rate of deduction for depreciation, $198.02, instead of $350, contended for by petitioner presumably on the assumption that the respondent having previously considered the cost and value as $5,000 was bound thereby and estopped from reaching a different finding and determination, although it was never shown at what date the furniture and fixtures were acquired by the partnership or that their cost was in fact more than $3,480.20 ultimately determined by respondent. The burden of making a full and satisfactory showing touching the cost and deduction claimed, the age, condition and remaining useful life, etc., of the assets in question, rested upon the petitioner and we find and determine were not satisfactorily shown by petitioner, and therefore we sustain the action of the respondent with respect to this issue. See T. D. 4422 and section 23

(k) of the Revenue Act of 1932 and article 165 of Regulations 69, 65 and 62 as amended, which in part states the following: [49]

> * * * The deduction for depreciation in respect of any depreciable property for any taxable year shall be limited to such ratable amount as may reasonably be considered necessary to recover during the remaining useful life of the property the unrecovered cost or other basis. The burden of proof will rest upon the taxpayer to sustain the deduction claimed. Therefore, taxpayers must furnish full and complete information with respect to the cost or other basis of the assets in respect of which depreciation is claimed, their age, condition and remaining useful life, the portion of their cost or other basis which has been recovered through depreciation allowances for prior taxable years, and such other information as the Commissioner may require in substantiation of the deduction claimed.

V. The next question is whether the Commissioner erred in determining deficiencies against the petitioner by adding, under section 104, Revenue Act of 1932[1], 50 per cent, and under section 102,

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[1]Sec. 104. Accumulation of Surplus to Evade Surtaxes.

(a) If any corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its

Revenue Act of 1934, 25 per cent, of net income as defined in subsection (c). The Commissioner made his determination under sections 104 and 102 as follows:

Year	Net Income under Section 21	Dividends added	Total or Net Income adjusted under 104(c) [or 102(c), Revenue Act of 1934]	Tax Liability at 50% under 104(a) [or 25% under 102(a), Revenue Act of 1934]
1932	$ 3,473.50	$18,258.00	$21,731.50	$10,865.75
1933	20,874.51	17,541.00	38,415.51	19,207.76
1934	19,014.25	25,057.00	44,071.25	11,017.81

[50]

The facts so far as material on this question may be summarized, and we find as follows: Petitioner was organized to engage in the business of logging,

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gains and profits to accumulate instead of being divided or distributed, there shall be levied, collected, and paid for each taxable year upon the net income of such corporation a tax equal to 50 per centum of the amount thereof, which shall be in addition to the tax imposed by section 13 and shall be computed, collected, and paid upon the same basis and in the same manner and subject to the same provisions of law, including penalties, as that tax.

(b) The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to escape the surtax.

(c) As used in this section the term "net income" means the net income as defined in section 21, increased by the sum of the amount of the dividend deduction allowed under section 23 (p) and the amount of the interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner.

* * * * * * *

manufacture, purchase, sale and transportation of lumber, and operation of steamships. The steamers Oregon and Idaho were acquired in January 1929, were operated by the petitioner for about six months and were then laid up, and had not again been put into operation at the close of the taxable years. Some lumber and allied business was carried on. The corporation always had the purpose of reengaging in the lumber and shipping business. The partnership which had preceded the corporation had about $1,500,000 in the logging, lumbering and milling business and it would have required about that much capital at the time of the hearing. The petitioner did not reenter the lumber-logging-milling business prior to or during 1932, 1933 and 1934, because the losses were heavy in the logging business, the sawmills were taking big losses, business was depressed, no building was going on and it was very hard to sell lumber, and it would have been unprofitable to go into a business which was losing money. The petitioner reported in Federal income tax returns gross sales as follows: 1932—$28,725.96; 1933—$92,262.09; 1934—$170,239.51. Net losses were reported by petitioner as follows: 1932—$11,740.89; 1933—$1,341.36; 1934—$118.75. The petitioner had during the taxable years a net loss from its operations other than ownership of stocks. It had income, however, from dividends on stocks of domestic corporations, and reported under that heading, and deducted, as follows: 1932—$18,258; 1933—$17,541; 1934—$25,057. On balance sheets attached

to the income tax returns undivided profits (elsewhere in the returns for 1932 and 1933 referred to as "surplus and undivided profits") were reported as of December 31 in each taxable year as follows: 1932—$19,309.75; 1933—$36,732; 1934—$25,447.64.

[51]

The income tax returns showed common stock on January 1 of the years from time of incorporation, as follows:

1929	$696,000	1932	$2,500,000
1930	746,000	1933	2,500,000
1931	800,000	1934	2,500,000

Common stock as of December 31, 1934, was returned as $2,535,000. The only stock ever issued was $1,000, to W. T. Wilson and F. A. Wilson, for $500 paid by each on December 31, 1928.

Capital contributions of cash were from time to time made by F. A. Wilson and W. T. Wilson. With such constributions the petitioner purchased securities, in practically all cases stocks of domestic corporations. All stocks were purchased by the corporation for cash. No stocks or bonds were transferred by W. T. Wilson or F. A. Wilson to the corporation. The income tax returns filed by petitioner and its records, as placed in evidence, do not agree in important particulars. The income tax returns in part show as follows:

	December 31		
	1932	1933	1934
Assets			
Cash	$1,106,377.07	$1,022,123.45	$ 972,147.49
Securities of Domestic Corporations	1,000,943.50	1,032,190.55	1,077,778.05
Liabilities			
Notes payable	200,000.00	—	—
Common stock	2,500,000.00	2,500,000.00	2,535,000.00

However, we find that the petitioner included in the amounts returned as cash, for each of said taxable years, I.O.U.'s in large amounts, and we find the facts to be as follows, with respect to the respective items above set out: [52]

	December 31		
	1932	1933	1934
Assets			
Cash, as shown by Account Books and records	$ 96,638.23	$ 9,186.43	$ 73,707.36
Securities of Domestic Corporations as shown by Books of account and Record			
(cost)	750,943.50	782,190.55	837,778.05
" (market value)	439,961.87	777,792.00	810,797.75
Liabilities			
Notes payable as shown by record	—	—	—
Common stock per record	1,000.00	1,000.00	1,000.00

The petitioner's records carried no item of $200,000 notes payable, though such item appeared in the income tax returns for 1929, 1930, 1931, and 1932. The petitioner kept no record of petty cash, and no account of the I.O.U.'s placed in the cash box by W. T. Wilson and F. A. Wilson. At the

time of trial petitioner's cash box contained one I.O.U. for $843,438.54, consisting of two equal items, one purportedly due from W. T. Wilson and the other from F. A. Wilson. A certified public accountant who testified for petitioner attempted to take a trial balance from petitioner's general ledger as of January 1, 1932, December 31, 1932, December 31, 1933, and December 31, 1934, but was unable to do so because the general ledger accounts lacked other accounts necessary to a complete balance of the records. Francis Wilson, an officer of the company, furnished the accountant necessary information as to identity of additional accounts and a balance of the books was then completed. On January 31 (year not shown) the books show "transfer from treasury stock $10,000." W. T. Wilson testified that "we put in that much cash to take it up." The ledger of the corporation carried two accounts headed "treasury stock," totalling $250,000, but there was in fact [53] no treasury stock. The corporate books do not show the years, though dates of days and months appear. No dividends or salaries to officers were paid by the petitioner from incorporation until after the end of the taxable years here in question.

W. T. Wilson paid about $150 Federal income tax in 1932, and none in 1933 and 1934. F. A. Wilson paid none for 1932, 1933 and 1934.

Petitioner's books showed accounts receivable from F. A. Wilson as follows:

Year	Charges	Credits	Net Due December 31
1933	$82,597.77	$39,363.40	$43,234.37
1934	62,199.38	69,821.25	35,612.50

On January 2, 1935, F. A. Wilson was credited with $35,612.50 by purchase of Kennecott Copper stock.

The general ledger trial balances showed accounts receivable from F. A. Wilson to be $28,091.96 on December 31, 1933. "W. Wilson" is shown as owing accounts receivable on December 31 of the taxable years 1932, 1933 and 1934, in the following respective amounts: $17,717.88, $16,917.88, $16,-917.88.

What do the facts above epitomized signify with reference to purpose to escape surtax within the purview of section 104 of the Revenue Act of 1932 and section 102 of the Revenue Act of 1934? Patently the record is unsatisfactory and often contradictory, and the corporate books kept in no normal manner.

First, we hold that the corporation was not FORMED for the purpose interdicted by the above sections. The parties have stipulated that petitioner was incorporated "to take over and continue the business of said co-partnership." This indicates a business purpose in formation of the [54] corporation. For a short time, about five or six months, after formation of the corporation and acquisition of the two steamers in January 1929, the corporation operated the steamers. Shortly thereafter came the financial crash of October 1929. We are not

prepared to say that the two incorporators at the inception of this corporation formed it for the purpose involved in the statutes under consideration.

Was the corporation AVAILED OF during 1932, 1933 and 1934 for the purpose of preventing imposition of surtax upon its two stockholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed? The respondent so considered in determining the tax as set forth in the deficiency notices, and the burden is upon the petitioner to show to the contrary. Chicago Stock Yards Co., 41 B. T. A. ..... (No. 87, March 20, 1940). Though the petitioner was not, in our opinion, a "mere" holding or investment company, within the statutory phrase we find it to be, during the taxable years, primarily such a holding or investment company. Actual business operations were comparatively small. No cash book was kept because transactions were too few and too small, and vouchers were used instead. The boats were laid up long before the taxable years, and net loss from business operations (except ownership of securities) was taken each taxable year. No dividends were paid. No salaries were paid to officers. At the same time, the two sole stockholders contributed large amounts of cash to their corporation. The evidence of one of the stockholders indicates that such contributions of cash and other assets amounted to $1,279,314.24. We are unable to make such finding of fact, for the record is to a considerable extent contradictory and it is plain that

the testimony of the witness can not be accepted herein at face value. [55]

The witness, W. T. Wilson, testified that in the month of incorporation, December 1928, $695,000 in cash and other assets was put into the corporation, that $50,000 was added about January 1, 1929, that in January 1930, $54,000 was contributed, making a balance of $800,000 on January 1, 1931, that during January 1931, $480,312.24 which he and his brother had in a San Francisco bank was added (in addition to $1,700,000 in I.O.U.'s), that $35,000 was transferred from profit and loss into the surplus account, and then from book surplus to capital, but that there was a net loss from operations. Explaining the increase in cash from $56,593.58 on December 31, 1930, to $1,642,298.24 on December 31, 1931, he said "Oh, we just put a few I.O.U.'s in the cash box," and that a large part of the difference was I.O.U.'s; that they used I.O.U.'s right along; that he kept corporate books and they balance every year perfectly. However, W. T. Wilson and his brother, the only other stockholder, for four consecutive years swore to income tax returns of the petitioner, stating cash in large amounts—up to about $1,000,000—which the corporation did in fact not possess, and which the witness at the hearing explained as I.O.U.'s from his brother and himself. At the time of hearing, petitioner's cash box still contained such an I.O.U. in the amount of $843,-438.54. The same oaths represented for four consecutive years that the petitioner owed notes pay-

able of $200,000, contrary to the fact, represented stocks of domestic corporations to be about $250,000 more than was the fact, and for six years represented common stock to be from $696,000 to $2,535,000 when in fact it was $1,000. One sworn statement appears to have equal weight with another, particularly when all are with reference to the same proposition—petitioner's income taxes. Evan V. Quinn et al., 26 B. T. A. 970. It is apparent, however, from the bank [56] books, that the two stockholders did contribute large amounts in cash to the petitioner and made other contributions of assets. With the money, stocks, principally, if not wholly, of domestic corporations, and some bonds were purchased. In the taxable years the dividends received from domestic corporations were deducted.

Was the purpose of the individuals to escape surtax by causing the corporation to accumulate its gains and profits? It did so accumulate its undivided profits through the taxable years. Petitioner argues that such accumulation was within the reasonable needs of its business, that the former partnership had had about $1,500,000 invested, and that the same was reasonably necessary. The evidence does not, we think, bear out petitioner's contention. The witness above referred to said that the same amount would be necessary "today," i. e., at the date of hearing, in 1939. What the reasonable requirements of the business were in 1932, 1933 and 1934 is left by the record to conjecture. Indeed, what little is shown as to the taxable years indi-

cates that there was no reasonable business need for the accumulations, for W. T. Wilson when asked to explain "why you did not reenter such business before the years '32, '33 and '34, or during those years," responded that in the logging business losses were heavy, that in the manufacture of lumber the sawmills were taking big losses and "It would be unprofitable to go into a business which was losing business." Elsewhere he said that business was depressed, no building was going on and that it was very hard to sell lumber. Again he testified to the purpose "to reengage" in the shipping and lumber business. Though these statements almost put the company out of business in the taxable years, we think that such can not fairly be said, for some business was conducted. They do, however, in [57] our opinion, prove an intent not to reenter a losing business during the period of such losing business and depression, and demonstrate that the small undivided profits accruing largely from security holdings can not reasonably be said to have been accumulated as a reasonable business necessity. There is no evidence as to how the money would be expended, or of any intent to go into business to the same extent as had the partnership a few years earlier. A mere comparison with an earlier partnership business constitutes no sufficient showing of the financial needs of the corporation in the taxable years. Petitioner disproves, rather than proves, reason for not paying dividends during the taxable years. It might have been that looking into

the long future and comparing with the business of the partnership in 1928 and earlier years, the petitioner's officers might have wished to accumulate, not only the capital contributions, and securities in which they were invested, but the undivided profits from dividends from domestic corporations. But we think no showing has been made of any immediate, or reasonably immediate, need for conserving both the large amounts of securities and the comparatively small amount of undivided profits. It can not reasonably be thought, with the depression so seriously affecting the shipping and lumber industry as petitioner shows, that the company would suddenly find conditions so changed as to require liquid assets to the full extent of not only its large assets, but its current gains and profits. After a painstaking study of the often confusing and contradictory record, we come to the conclusion that the petitioner has not adduced the proof necessary to meet its burden of proof. This conclusion is strengthened by the manner in which the corporation dealt with its two sole stockholders. If there was reasonable business reason to accumulate the undivided profits, why was F. A. Wilson permitted to have credit as shown by accounts receivable from him of $43,234.37 at the end of 1933 when undivided profits were reported as $36,732, and of $35,612.50 at the end of [58] 1934 when undivided profits were reported as $25,447.64? It is plain that the two stockholders dealt with their corporation much as they desired. There is no showing of the financial

responsibility of F. A. Wilson for the credit he enjoyed from his corporation. Indeed, no consistent record was even kept of the matter. Though an account receivable set up as to him individually showed the above figures, on the general ledger trial balances placed in evidence, he is listed among bills receivable with $28,091.96 as the amount on December 31, 1933—instead of $43,234.37 as above seen, and on the list of accounts receivable of petitioner as at December 31, 1933, placed in evidence by petitioner, no item as to F. A. Wilson appears. Likewise, "W. Wilson," whom we think it reasonable in the absence of explanation to assume to be W. T. Wilson, the other stockholder, also owed the corporation as follows: December 31, 1932—$17,717.88; December 31, 1933—$16,917.88; December 31, 1934—$16,917.88. He reduced the amount only $800 in two years. In our opinion the petitioner presents a picture similar in outline to that in Rands, Inc., 34 B. T. A. 1094, where we commented upon the financial dealings between a sole stockholder and his corporation and the fact that had he employed his funds instead of lending them to the corporation, he would have had substantial taxable income. The categoric denial of intent to avoid surtax, by the Witness W. T. Wilson, must be compared with his earlier sworn statements in the income tax returns and the manner in which petitioner's books were balanced perfectly by use of fictitious cash, common and treasury stock and notes payable. We hold that the petitioner was availed of in the taxable

years for the purpose of preventing imposition of surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed. [59]

VI. The respondent further determined as to each taxable year that the petitioner was subject to the 5 per cent negligence penalty under section 293 of the Revenue Acts of 1932 and 1934. The facts above set forth and reviewed in connection with the discussion of section 104 are here applicable with at least equal force. The remarkable way in which the petitioner kept its record and made its returns, setting up false statements as to large amounts of cash as to notes receivable and as to amount of capital stock, maintaining no cash book, and no record of I. O. U.'s owing by its stockholders, requires the application of the negligence penalty. The cases cited by petitioner as to honest mistake or misunderstanding do not apply to books kept in the manner prescribed by the principal witness herein. Obviously, a part of the deficiency was due to "negligence or intentional disregard of rules and regulations" without which the tax in this case could have been ascertained without all of the difficulty encountered. We hold that the Commissioner did not err in the application of the 5 per cent negligence penalty under section 293.

Decision will be entered under Rule 50.

Enter:

Entered May 22, 1940. [60]

United States Board of Tax Appeals
Washington

Docket No. 93668.

WILSON BROTHERS & CO.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION.

Pursuant to the Memorandum Opinion of the Board entered May 22, 1940, the respondent herein having on June 20, 1940, filed a recomputation of the tax, and the petitioner having on July 22, 1940, filed an acquiescence in said recomputation, now, therefore, it is

Ordered and decided: That there are deficiencies in normal tax and surtax and a penalty for the year 1934 as follows:

Normal Tax—$1,912.05.

Additional Tax under section 102, 1934 Act—$9,740.70.

Penalty—$582.63.

Enter:

[Seal] (Signed) R. L. DISNEY,
Member.

Entered Aug. 6, 1940. [61]

[Title of Board and Cause.]

PETITION FOR REVIEW OF DECISION OF THE UNITED STATES BOARD OF TAX APPEALS BY THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

To the Honorable, The Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Wilson Brothers and Company (properly entitled Wilson Bros. & Co.), your petitioner, pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code respectfully petitions this Honorable Court to review the decision of the United States Board of Tax Appeals entered on the 6th day of August, 1940, and finding deficiences in income tax, together with additional tax under Section 102 of the Revenue Act of 1934, and a negligence penalty under Section 293(a) of said Act in the total of $12,235.38 for the taxable calendar year 1934. [62]

I.

Jurisdiction

Your petitioner is a corporation organized under the laws of the State of Nevada, having, during the taxable years involved, its principal office and place of business in the City and County of San Francisco, State of California. Petitioner timely filed its Federal income tax returns in respect to which the aforementioned tax liabilities arose with the Collector of Internal Revenue, 1st District of California, located in the City and County of San Fran-

cisco, State of California, which is situated within the jurisdiction of the United States Circuit Court of Appeals for the Ninth Judicial Circuit.

II.

Prior Proceedings

The Commissioner of Internal Revenue, by his letter dated December 30, 1935, asserted a deficiency in petitioner's tax liability for the year 1932 in the sum of $11,343.36 and a penalty of five percentum in the amount of $567.17, he also asserted a deficiency in petitioner's tax liability for the year 1933 in the sum of $22,078.01 and a penalty of five per centum in the amount of $1,103.90. By his letter of March 8, 1938, the Commissioner asserted a deficiency in petitioner's tax liability for the year 1934 in the sum of $13,632.27 and a penalty of five percentum in the amount of $681.61.

Thereafter, and within the times prescribed by law, the petitioner filed with the United States Board of Tax Appeals its petitions under the aforesaid two letters requesting the redetermination of such deficiences. The proceedings duly came on for hearing on June 6, 1939, at which time the two pro- [63] ceedings were consolidated for hearing. The proceedings were submitted to the Board upon a written stipulation of facts, oral testimony of witnesses and documentary evidence applicable to the two proceedings.

Thereafter, and on May 22, 1940, the United States Board of Tax Appeals made its report and rendered a memorandum opinion, through a single

member sitting as Division No. 4 of said Board, approving in part the determinations of the Commissioner.

Thereafter and on August 6, 1940, decisions were made and entered in each of the two proceedings by the United States Board of Tax Appeals whereby final orders of redetermination of deficiencies for the respective years involved were made and entered as follows:

Year	Normal Tax	Additional Tax Under Section 104, 1932 Act and Section 102, 1934 Act	Penalty
1932	None	$ 3,316.84	$165.84
1933	$1,499.93	14,224.80	786.24
1934	1,912.05	9,740.70	582.63

III.

Statement of the Nature of the Controversy

This proceeding is for the year 1934 (Docket No. 93368) and involves income taxes, together with surtax alleged under the provisions of Section 102 of the Revenue Act of 1934 and a five percentum penalty for asserted negligence under Section 293(a) of said Act, for the taxable calendar year 1934.

The controversy between petitioner (appellant before the Court) and the Commissioner of Internal Revenue involves several issues which, for the years involved, will be presented [64] in the order in which they are discussed in the report or memorandum opinion of the Board of Tax Appeals.

1. (Issue III(a) in the report memorandum opinion) Whether petitioner was entitled to write

off and deduct as a partially worthless or bad debt for the taxable year 1934 the amount of $5,000. from the sum of $43,276.06 owed to it by the Woodhead Lumber Co. of California.

2. (Issue III(c) in the report or memorandum opinion) Whether petitioner was entitled to write off and deduct as a partially worthless or bad debt for the taxable year 1934 the amount of $5,500. with respect to bonds of Kentucky Fuel Gas Corporation, a bankrupt corporation.

3. (Issue IV(a) in the report or memorandum opinion) Whether the basis for depreciation of petitioner's 75% interest in the steamship "Idaho" adjusted to January 1, 1932 is $52,466.67 as determined in the memorandum opinion, or $91,466.67. This issue is one of law and arises from the difference between the cost ($40,000) of said interest to Henry Wilson and its value $79,000) on February 6, 1917 when he made a gift thereof to his wife, Mary H. Wilson, who in turn made a gift thereof to petitioner on January 2, 1929.

4. (Issue V in the report or memorandum opinion) Whether the petitioner corporation was availed of during the taxable years involved for the purpose of preventing imposition of surtax upon its two shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed.

5. (Issue VI in the report or memorandum opinion) Whether the petitioner was subject to the five per centum negligence [65] penalty under Section 293(a) of the Revenue Act of 1934.

Due in part to the fact that the report or memorandum opinion of the Board subdivides its findings as it subdivides its opinion on the several issues, thereby disregarding findings of fact made on some issues material to other issues, a consideration of the evidence as well as a consideration of all of the facts found is necessarily involved in the review of the Board's decision.

IV.

Assignments of Error

In assigning the errors which petitioner believes to have been committed by the United States Board of Tax Appeals, assignment is made in the order in which the issues were decided and numbered in the report or memorandum opinion of the Board entered May 22, 1940, for the two proceedings docketed and numbered 83,397 and 93,668. For convenience of reference, the issues as considered in the report or memorandum opinion are designated by the Roman numerals, employed in subdividing said report or memorandum opinion into separate parts. No assignments of error are made to issues I and II considered in said report or memorandum opinion.

Petitioner assigns as error the following acts and omissions of said United States Board of Tax Appeals:

III.

(1) The failure to find and determine that the $43,276.06 account receivable due from the Woodhead Lumber Co. of California was impaired during the year 1934 in at least the amount ($5,000.00)

charged off by petitioner in said year against said account as a partial bad debt. [66]

(2) The failure to find and determine that petitioner had fully met its burden of proving error on the part of respondent in disallowing the claimed deduction of such partial bad debt, such disallowance being predicated entirely on the false assumption that no direct write-off had been made of said $5,000.

(3) The making of a purported finding of fact contrary to the evidence, record and issue involved as follows:

> "Upon consideration of the entire record we find and determine that the alleged worthless character of the debt from the Woodhead Lumber Co. of California has not been shown. We therefore find and hold that the Commissioner did not err in disallowing the $5,000 deduction claimed."

(4) The failure to find that the cost to petitioner of its bonds of the Kentucky Fuel Gas Corporation were impaired during the year 1934 in at least the amount ($5,500) charged off by petitioner in said year against the cost of said bonds as a partial bad debt.

(5) The failure to find and determine that petitioner had fully met its burden of proving error on the part of respondent in disallowing the claimed deduction of such partial bad debt, such disallowance being entirely predicated entirely on the false assumption that no direct write-off had been made of said $5,000.

(6) The making of a purported finding with respect to the deduction of said $5,500 contrary to the evidence, record and issue involved as follows:

> "Obviously such a record does not show error on the part of the Commissioner in denying the deduction."

IV.

(7) The failure to allow as a basis for depreciation on the Steamship "Idaho" from January 1, 1932, the amount of $91,377.78 [67] and to determine that petitioner was entitled to deduct depreciation on said steamship for each of the taxable years 1932, 1933 and 1934 in the amount of $6,100.77 per annum.

(8) The failure to allow as a part of the basis of depreciation of the Steamship "Idaho" from January 1, 1932, the amount of $79,000. as the fair market value of a twenty per cent interest therein given to Mary H.Wilson on February 6, 1917, by her husband, at which time said steamship had a fair market value of $395,000., which said twenty per cent interest was donated to petitioner by said Mary H. Wilson on January 2, 1929.

(9) The determination that the basis (unadjusted) of property acquired by gift prior to December 31, 1920 is changed from the value at the time of said gift to cost to the donor of said gift when said property is made the subject matter of a gift by said donee after December 31, 1920.

V.

(10) The making of a purported finding with respect to all of the taxable years involved and with-

out discrimination between the circumstances and facts relating to each of the years 1932, 1933, and 1934, to the effect:

> "We hold that the petitioner was availed of in the taxable years for the purpose of preventing imposition of surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed."

when in fact the record and that part of the record considered in the report or memorandum opinion with respect to such finding is contrary to such finding and said finding is inconsistent with other findings upon which it is purportedly based.

(11) The determination that for the taxable year 1932 petitioner is liable under the alleged authority of Section 104(a) of the [68] Revenue Act of 1932 in the amount of $3,316.84 as a surtax for the alleged accumulation of surplus contrary to the provisions of said section.

(12) The determination that for the taxable year 1933 petitioner is liable under the alleged authority of Section 104(a) of the Revenue Act of 1932 in the amount of $14,224.80 as a surtax for the alleged accumulation of surplus contrary to the provisions of said section.

(13) The determination that for the taxable year 1934 petitioner is liable under the alleged authority of Section 102(a) of the Revenue Act of 1934 in the amount of $9,740.70 as a surtax for the alleged accumulation of surplus contrary to the provisions of said section.

(14) In making the determinations complained of in assignments 10 to 13 hereof inclusive, the failure to consider the true earned surplus of petitioner as distinguished from its taxable earnings and profits as determined in the report or memorandum opinion.

(15) In making the determinations complained of in assignments 10 to 13 hereof, inclusive, the failure to make any finding as to what surplus, if any, petitioner had accumulated in each of the taxable years involved.

VI.

(16) The determination that for the taxable year 1932 petitioner is liable for a negligence penalty under the alleged authority of Section 293(a) of the Revenue Act of 1932 in the amount of $165.84, when the record does not disclose that any part of the deficiency determined was "due to negligence or intentional disregard of rules and regulations". [69]

(17) The determination that for the taxable year 1933 petitioner is liable for a negligence penalty under the alleged authority of Section 293(a) of the Revenue Act of 1932 in the amount of $785.24, when the record does not disclose that any part of the deficiency determined was "due to negligence or intentional disregard of rules and regulations".

(18) The determination that for the taxable year 1934 petitioner is liable for a negligence penalty under the alleged authority of Section 293(a) of the Revenue Act of 1934 in the amount of $582.63, when the record does not disclose that any part of the de-

ficiency determined was "due to negligence or intentional disregard of rules and regulations".

General

(19) The failure to make comprehensive and generally applicable findings of facts which would apply equally to all issues involved in the proceedings and be adequate for proper determination of all the issues involved.

(20) The setting forth separately in the report or memorandum opinion in connection with the discussion and determination of each of the issues involved therein of inadequate facts to support the conclusions reached in such opinion on the majority of said issues.

(21) The severance of facts in the relation to each of the issues discussed and determined in the report or memorandum opinion so that purported findings with regard to one issue do not have application to the other issues involved.

(22) The determination of separate issues without regard to facts found to be true with respect to other issues involved in the proceedings. [70]

(N.B. The errors numbered 19, 20, 21 and 22 are manifest from a reading of the report or memorandum opinion on the various numbered issues and from the following express language of the opinion:

"Certain issues as to depreciation upon wooden buildings and automobiles have been settled by stipulation which will be reflected in decision under Rule 50. The other issues will be

considered in the order above set forth, *the facts*, except the general facts as to incorporation stated above, *being set forth separately in connection with the discussion of each issue.* (Italics supplied.)

(23) The intermingling of findings of fact, conclusions as to facts and conclusions of law in such manner as to render the decision of the Board in its report or memorandum opinion arbitrary and theoretical.

(24) In making its findings of fact and conclusions of law therefrom the Board failed to make findings of fact in conformance with the evidence.

Wherefore, the petitioner prays that the decision of the United States Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit; that a transcript of the record be prepared in accordance with law and the rules of said Court for filing, and that appropriate action be taken to the end that the errors complained of herein be reviewed and corrected by said Court.

WILSON BROS. & CO.
By FRANCIS A. WILSON,
President.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Counsel for Petitioner
1110 Balfour Building,
San Francisco, California. [71]

State of California,
City and County of San Francisco—ss.

Francis A. Wilson being first and duly sworn says, I am president of Wilson Bros. & Co., the petitioner and appellant above-named; that I have read the foregoing petition for review and know the contents thereof and the facts set forth therein are true as I verily believe; that said petition is filed in good faith and not for purposes of delay.

FRANCIS A. WILSON

Subscribed and sworn to before me this 29th day of October, 1940.

[Seal] ELEANOR J. SMITH,
Notary Public in and for the City and County of San Francisco, State of California.

My commission expires Dec. 31, 1942. [72]

[Endorsed]: U. S. B. T. A. Filed Oct. 31, 1940.

[Title of Board of Cause.]

AFFIDAVIT OF SERVICE BY MAIL

Louis Janin, being first duly sworn, deposes and says:

That he is a citizen of the United States, and over the age of 21 years, and not a party to the above-entitled proceedings. That on this 30th day of October, 1940, he deposited in the United States Post Office in San Francisco, California, addressed to the Commissioner of Internal Revenue, Internal Reve-

nue Building, Washington, D. C., a copy of petition for review in the above-entitled proceedings, together with a notice of mailing petition for review, addressed to said Commissioner of Internal Revenue, and to John P. Wenchel, Chief Counsel, Attorney for Commissioner. That said copy of petition and notice for filing petition were enclosed in an envelope addressed to the Commissioner of Internal Revenue, Internal Revenue Building, Washington, D. C., with air mail postage prepaid thereon for immediate and prompt delivery.

LOUIS JANIN.

Subscribed and sworn to before me this 30th day of October, 1940.

[Notarial Seal] EDITH VIA,

Notary Public in and for the City and County of San Francisco, State of California.

[Endorsed]: U. S. B. T. A. Filed Oct. 31, 1940. [73]

[Title of Board and Cause.]

To Commissioner of Internal Revenue, and to John P. Wenchel, Chief Counsel, Attorney for Respondent, Bureau of Internal Revenue Building, Washington, D. C.:

You are hereby notified that on this 31st day of October, 1940, a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of the United States Board of

Tax Appeals, heretofore rendered in the above-entitled cause, was mailed by air mail to the Clerk of said Board. A copy of the petition as filed is attached hereto, and served upon you.

Dated: This 30th day of October, 1940.

ADOLPHUS E. GRAUPNER
LOUIS JANIN

Service of the foregoing notice of filing and of a copy of the petition for review is hereby acknowledged this 31st day of October, 1940.

J. P. WENCHEL
Chief Counsel, Bureau of
Internal Revenue,
Attorney for Respondent.

[Endorsed]: U. S. B. T. A. Filed Nov. 1, 1940. [74]

[Title of Board and Cause.]

STATEMENT OF POINTS ON WHICH PETITIONER INTENDS TO RELY

In compliance with paragraph (d) of Rule 75 of the Rules of Civil Procedure for the District Court of the United States as made applicable for review of a decision of the United States Board of Tax Appeals by Rule 30 of the Rules of the United States Circuit Court of Appeals for the Ninth Circuit the above-named petitioner herewith states the points on which it intends to rely on the pending

petition for review of the decision of said Board in the above-entitled proceeding.

Petitioner will rely upon all of the assignments of error set forth in the petition for review of decision in the above-entitled proceedings by the United States Circuit Court of Appeals for the Ninth Circuit filed with the United States Board of Tax Appeals on October 31, 1940.

With respect to the above-entitled proceeding involving the taxable calendar year 1934 and, as a necessary incident the [75] years 1932 and 1933 a concise statement of the points involved in the appeal is as follows:

1. The Board erred in determining that for the year 1934 petitioner was not entitled to write-off and deduct as a partial bad debt the amount of $5,000 of a total of $43,276.06 owing to it from the Woodhead Lumber Co. of California.

2. The Board erred in determining that for the year 1934 petitioner was not entitled to write-off and deduct as a partial bad debt at least the amount of $5,500 on the impaired value of bonds of the Kentucky Fuel Gas Corporation.

3. The Board of Tax Appeals erred in failing to allow petitioner a valuation, as a basis for depreciation on the Steamship "Idaho" from January 1, 1932, of the amount of $91,377.78 and to determine that petitioner was entitled to deduct depreciation on said steamship for each of the taxable years 1932, 1933 and 1934 in the amount of $6,100.78 per annum. Such error resulted from failure to deter-

mine as a part of the basis of depreciation, the amount of $79,000 as the fair market value of a twenty per cent interest in said steamship given to Mary H. Wilson on February 6, 1917, and by her donated to petitioner on January 2, 1929.

4. The Board of Tax Appeals erred in finding with respect to all the taxable years involved, viz: 1932, 1933 and 1934, as follows:

> "We hold that the petitioner was availed of in the taxable years for the purpose of preventing imposition of surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed."

and further erred in determining that for the year 1932 petitioner is liable under Section 104(a) of the Revenue Act of 1932 for [76] $3,316.84 as a surtax for alleged accumulation of surplus; also, it further erred in determining that for the year 1933 petitioner is liable under the aforesaid section for $14,-224.80 as a surtax for alleged accumulation of surplus; also, it further erred in determining that for the year 1934 petitioner is liable under Section 102(a) of the Revenue Act of 1934 for $9,740.70 as a surtax for the alleged accumulation of surplus.

In making such determinations the Board failed to consider petitioner's true earned surplus as distinguished from its taxable earnings and profits as determined in the report or memorandum opinion and, also, failed to make any findings as to what

surplus, if any, petitioner had accumulated in each of the taxable years involved.

5. The Board erred in determining that for the taxable year 1934 petitioner is liable for a negligence penalty under Section 293(a) of the Revenue Act of 1934 when the record does not disclose that any part of the deficiency determined in said year was "due to negligence or intentional disregard of rules and regulations."

6. The Board erred in failing to make comprehensive or general finding of facts applicable to all issues involved and further erred in segregating and separating the findings made so that findings made on one issue, although properly material and applicable to other issues, are made inapplicable to other issues to which they are material and controlling as is evidenced by the following preliminary statement in the report or memorandum opinion.

> "Certain issues as to depreciation upon wooden buildings and automobiles have been settled by stipulation which will be reflected in decision under Rule 50. The other issues will be considered in the order above set forth, *the facts,* except the general facts as to in- [77] corporation stated above, *being set forth separately in connection with the discussion* of each issue." (Italics supplied).

The Board further erred in failing to make findings of fact in conformance with the evidence, and in intermingling, as findings of fact, facts, conclusions

as to facts, and conclusions of law in such manner as to conflict with the record and the law.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for Petitioner,
1110 Balfour Building,
San Francisco, California.

Admission of service of the foregoing statement of points on which petitioner intends to rely is hereby admitted this 11th day of March, 1941.

J. P. WENCHEL
Chief Counsel, Bureau of Internal Revenue,
Attorney for Respondent on Review.

[Endorsed]: U. S. B. T. A. Filed March 11, 1941.

[78]

United States Board of Tax Appeals
Docket No. 83397 and Docket No. 93668

WILSON BROTHERS and COMPANY (Wilson Bros. & Co.), a corporation,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

REVISED STATEMENT OF THE EVIDENCE

The above entitled and numbered proceedings came on for consolidated hearing before the Honorable Richard L. Disney, Member of the United

States Board of Tax Appeals, on June 6th and 7th, 1939, at the City and County of San Francisco, State of California.

The following represents a narrative statement of the evidence submitted to said United States Board of Tax Appeals at said times and place.

A consolidated partial stipulation of facts was filed for both proceedings and the respective deficiency notices for the two proceedings were admitted in evidence and marked Petitioner's Exhibits No. 1 and 2. (These Exhibits are respectively Exhibits A to the two petitions on file in the [79] above entitled proceedings).

WINFRED T. WILSON

was called as a witness by and on behalf of the petitioner and having been first duly sworn testified on June 6th, 1939, in substance as follows:

Direct Examination

I am a shareholder and the secretary and treasurer of the petitioner corporation and am familiar with and identify the corporation's income tax returns for each of the calendar years 1932, 1933, and 1934. (Whereupon said returns were offered and admitted in evidence and marked respectively Petitioner's Exhibits No. 3, No. 4 and No. 5.) I was secretary and treasurer of the corporation during the years 1932, 1933 and 1934 and my brother Francis A. Wilson was the president. I performed the general duties of a secretary and treasurer and, in addition, kept the books.

(Testimony of Winfred T. Wilson.)

The corporation was organized in December of 1928 to engage in the logging business, the manufacture of lumber, the transportation of lumber, the operation of steamships as a part of the logging and lumber business, the buying and selling of lumber, and engaging in the general lumber business. My brother and I had been continuously and actively engaged in the lumber business since 1906.

It was never intended that the corporation was to be organized as a holding investment company. My brother and I never discussed the element of taxation as a reason for forming [80] the corporation. Subsequent to the year of organization of the corporation, including the years 1932, 1933 and 1934, by brother and I never discussed the use of the corporation for any Federal tax purposes or for any special tax purposes. Nor during the years 1929 to 1934 inclusive did my brother and I discuss or reach any conclusion that the corporation was to be availed of for accumulating surplus or avoiding surtax.

No stock of the corporation was ever issued beyond the forty shares subscribed for by my brother and myself when the corporation was formed. The corporation never declared any dividends in either cash or stocks and paid no compensation to its officers from the time of its organization through the taxable years involved because the earnings were insufficient to pay dividends and the assets were impaired.

(Testimony of Winfred T. Wilson.)

I kept the books of account of the corporation during the years 1932, 1933 and 1934 and have such books with me. Here is the stock record and certificate book; the articles of incorporation and the corporate record of Wilson Brothers & Company; the bank books of the Crocker First National Bank, Wells Fargo Bank; statements of the Bank of America, Crocker First National Bank and Wells Fargo Bank; sales books for 1932, 1933 and 1934; the journal for those years, and the ledger. The books were kept on an accrual basis. We did not keep a cash book because the transactions were too few. Instead, when we sent out a bill for lumber we sent out two bills and when the customer paid he sent back one of the bills which was our [81] record of payment. Then the payment was entered in the ledger and deposited in bank. Where some customers did not send back bills, they sent us voucher checks and we kept the voucher on the end of the check. All cash received went into the bank accounts except now and then a small check would be cashed for petty cash. The vouchers received and the bank books took the place of the cash book. The journal was kept in such manner that it reflected the ordinary transactions made by the corporation, although it did not reflect all of the cash transactions, because the volume of business was so small that it was not necessary. The ledger reflected the business transactions of the corporation during the three years involved and correctly stated the cash

(Testimony of Winfred T. Wilson.)

position of the corporation at the opening and closing of each of said three years.

The witness was then shown a paper (afterwards admitted as Petitioner's Exhibit No. 6) prepared from the ledger, bank books and bank accounts, which showed the cash status of the corporation at the beginning and end of each of the years involved as follows:

Bank	1-1-32	12-31-32	12-31-33	12-31-34
San Francisco Bank	$403,750.00	$51,324.00	None	None
Crocker 1st Natl. Bk	–25.25	23,989.81	$ 539.04	$ 142.48
Wells Fargo Bank	320.83	21,324.42	8,647.39	21,415.06
Bank of America	259.79	None	None	52,149.82
Anglo-Cal. Natl. Bank	4,694.28	None	None	None
Total	$408,999.65	$96,638.23	$9,186.43	$73,707.36

[82]

Other than petty cash, the corporation had no money elsewhere than in the above-listed banks.

In the balance sheets forming a part of the income tax returns for the three taxable years involved cash was shown thereon as follows:

December 31, 1931	$1,642,498.24
December 31, 1932	1,106,377.07
December 31, 1933	1,022,123.45
December 31, 1934	972,145.49

The above cash statements contained in the returns were not correct and did not correspond with the cash position as shown in the ledger. The difference between the amounts shown in the ledger and those shown in the returns was represented by

(Testimony of Winfred T. Wilson.)

I.O.U.s which my brother and I placed in the cash box and carried as cash. Those I.O.U.s did not represent any money borrowed from the corporation and our intent in putting them into the cash box was that some day my brother and I might make enough money to pay them up and we would have a good sized corporation. We wanted to show a great deal of assets. From time to time my brother and I did make contributions on these I.O.U.'s. The money was deposited in bank, entries were made in the books. The amount paid in on an I.O.U. was deducted from it, showing a smaller I.O.U. In other words we destroyed one I.O.U. and then inserted the smaller one in its place. The cash position shown on the returns was out of balance with the cash position shown by the ledger and the bank account to the difference of [83] the face value of the I.O.U.s, and the amount of cash paid on such I.O.U.s.

The misstatement of the cash position on the second page of the corporation's returns in each of the taxable years did not effect its taxable income or the deductions from taxable income reported.

The witness was handed four papers or lists (afterward admitted as Petitioner's Exhibits Nos. 7, 8, 9 and 10) which he identified as the complete record of stocks of domestic corporations held and owned by petitioner as of January 1, 1932, December 31, 1932, December 31, 1933, and December 31, 1934.

(Testimony of Winfred T. Wilson.)

The costs shown on the lists, are the true costs of the stock to the corporation and correspond with the costs shown by the ledger entries. All of the stocks were acquired by purchase for cash. The approximate market values of the stocks set forth in the four lists at the beginning and end of each of the years involved, excepting the stock of Weeden & Co., were taken from the Financial Chronicle and other recognized journals recording sales and transactions in the stock and bond markets of the United States. The market value of the stock of Weeden & Co., which is not a listed stock, was obtained from that company which acts as broker in buying and selling its own stock for clients or buying for itself. The totals of cost and approximate market values of the stocks of domestic corporations owned by petitioner as shown by said Exhibits 7, 8, 9 and 10 for the opening and closing of each of the taxable years [84] herein involved are respectively as follows:—

Date	Cost	Approximate Market Value
January 1, 1932	$516,670.00	$273,115.12
December 31, 1932	750,943.50	434,961.87
December 31, 1933	782,190.55	777,792.00
December 31, 1934	837,778.05	810,797.75

The witness was handed a paper or list (afterward admitted as Petitioner's Exhibit No. 11, except as to data on bonds of Kentucky Fuel Gas Corporation) which he identified as showing all of the bonds owned by petitioner. The cost of the bonds

(Testimony of Winfred T. Wilson.)
shown on the list is the cost as shown by petitioner's ledger. The market value as of the respective dates was obtained from the brokers who sold the bonds to petitioner and checked against quotations of the market for the bonds in the New York Financial Chronicle. The totals of cost and market value of said bonds (exclusive of market value of Kentucky Fuel Gas. Corp. bonds) for the opening and closing of each of the taxable years as shown by said Exhibit 11 are as follows:

Date	Cost	Market Value
January 1, 1932	$ 3,975.00	$ 3,680.00
December 31, 1932	3,975.00	4,000.00
December 31, 1933	3,975.00	4,000.00
December 31, 1934	20,775.00	22,800.00

On January 2, 1929, Mary H. Wilson, W. T. Wilson and F. A. Wilson conveyed to petitioner a seventy-five percent [85] interest in the Steamship "Idaho" and a one-hundred percent interest in the Steamship "Oregon" as a contribution without consideration. (Bills of Sales of Enrolled Vessels for each of the interests so conveyed were admitted in evidence and marked Petitioner's Exhibit Nos. 12 and 13.) Mary H. Wilson, one of the grantors above named, was the mother of W. T. Wilson and Francis A. Wilson.

The vessels were acquired for the purpose of transporting lumber for the corporation and there was no intent to use those vessels for any other purpose. The vessels were employed in the lumber

(Testimony of Winfred T. Wilson.)

business for five or six months after January 2, 1929. Then business got very bad and we were unable to obtain cargoes that could be sold at a profit so we laid the vessels up.

Five or six months after January, 1929, we had a great panic or depression in the country and it continued in the lumber and shipping business through the years 1932, 1933 and 1934. The company continued its ownership of those ships during all that period for the purpose of operating them as soon as conditions would permit. During the three years in these proceedings involved the vessels were docked in the Oakland Estuary or the Alameda Estuary.

(The remainder of the testimony on pages 42 to 47 of the official report relates to deductions for maintenance of the vessels as found and allowed in issue II in the Memorandum Opinion of the Board, from which no appeal is taken.) [86]

(Testimony regarding additional interest claimed against petitioner on pages 48 and 49 of the reporters transcript of testimony is omitted because no appeal is taken from issue I in the Memorandum Opinion of the Board.)

During the years 1932 to 1934 the corporation charged off particular items as bad debts. The books showed a reserve for bad debts but that reserve was not in excess of the particular items charged off. (Testimony regarding a charge-off of $2,160. on account of the Steamship "Svea" follows

(Testimony of Winfred T. Wilson.)

on pages 51 to 55 is omitted because no appeal is taken on that item which forms part (b) of issue III in the Memorandum Opinion of the Board.)

On December 31, 1934, the corporation wrote off $5,000. as a partial loss on account of the financial condition of the Woodhead Lumber Company of California. I went to Los Angeles and went over the books of the company and found it was in very bad shape. There was a heavy mortgage on the assets. There was a bond issue of about $200,000. which came ahead of everything else. The bonds and the interest preceded the general creditors and that was on a specific piece of land. The balance of the assets consisted of accounts receivable which I judged "were no good". The improvements and the lumber business were on rented property which was held on a month to month basis and if it were thrown off that property those improvements would be practically worthless. The only hope of recovery was if business conditions kept on improving so the [87] company could make money they could pay out. After a careful examination of the books I determined that with the best advantage to the company our corporation would lose $5,000. and I wrote that amount off the corporation books in 1934 as being a reasonable deduction for partial loss on account of the Company's indebtedness to our corporation. We have never recovered that $5,000. Since 1934 the Woodhead Lumber Company of California went along as a business until it

(Testimony of Winfred T. Wilson.)

formed another corporation which took over a part of the assets. The old company started to lose some of their other assets through foreclosure and assignments due to agreements which it had and which preceded our account, in other words the company owned some houses on which there were mortgages and the mortgages were preferred against us so that a good many of the assets disappeared that way. The financial status of the company was worse in after years than at the time I investigated in 1934 and became steadily worse, it was in default on its bonds and was unable to pay the interest on the bonds.

In the year 1934 we charged off $5,500. as a partial loss on bonds of the Kentucky Fuel & Gas Corporation which our corporation owned. We made the charge-off because the company went into a receivership and it appeared that we would not recover the full amount but would take a loss in the amount charged-off. I made an investigation through the people who issued the bonds and that was their opinion. I had a list of the assets and liabilities of the corporation and in studying [88] the balance sheet it appeared that "there certain assets that were O. K. and that there would be some recovery due to that fact." I discussed the matter with my brother, the other stockholder of our corporation, and we reached the determination that the situation of the Kentucky Fuel & Gas Corporation looked pretty bad and that the amount of $5,500. should

(Testimony of Winfred T. Wilson.)

be written off as there was no way to get it back. We did not come to the conclusion that the bonds were entirely worthless; the bonds were a first mortgage on the property of the company and there must have been some residue for the bondholders because it was an operating company with considerable assets. That amount was written off in 1934.

(Testimony regarding deduction for depreciation of furniture and fixtures in pages 62 to 67 of the reporter's transcript is omitted because no appeal is taken on that issue which is decided as subdivision (c) of issue IV in the Memorandum Opinion of the Board.)

Petitioner was the owner of 75/100ths interest in the steamship "Idaho" and a 100 per cent interest in the Steamship "Oregon" during the taxable years involved. It was a practice of the shipping trade on the Pacific Coast during the years 1916, 1917, and 1918 and since that time to have vessels owned in shares and a fractional interest in a vessel was valued at its proportion to the value of the vessel as a whole. That is, a one-tenth share in a vessel would be equal in value to one-tenth of the vessel. [89]

On February 6, 1917, my father, Henry Wilson gave my mother, Mary H. Wilson a 20/100ths interest in the Steamship "Idaho" and 5/100ths interest to each of my brother, F. A. Wilson, and me, or a total of 30/100ths. The value of such interests on said date was in proportion to the value of the

(Testimony of Winfred T. Wilson.)

boat, which was $395,000. as set by the United States Board of Tax Appeals. These interests continued to be held by my mother, my brother and myself until January 2, 1929, when they were given "as a contribution without consideration" to the petitioner corporation. On January 6, 1924, my father gave my mother an additional 35/100ths interest in the Steamship "Idaho". The bill of sale (Exhibit A to Stipulation, marked for the record as Petitioner's Exhibit 15) recites a consideration of $10.00, but the transfer was a gift without consideration. In July, 1925, my brother and I each acquired an additional 5/100ths interest in the Steamship "Idaho" by purchase we paid a total of $11,-716.67 for the 10/100ths interest owned by Mr. Johnson, each of us paying one-half. This purchase gave each of my brother and me 10/100ths interest in the Steamship "Idaho" while my mother owned 55/100ths, making the seventy-five percent interest in the vessel which we transferred to the petitioner corporation on January 2, 1929, as "a contribution without any consideration".

On December 4, 1918, my father gave to each of my brother and me a 5/32ds interest in the wooden Steamship "Oregon". (Deeds of gift for 5/32nds interest in said vessel dated January 10, 1918, by Henry T. Wilson and Mary H. Wilson [90] to each of Winfred T. Wilson and Francis A. Wilson were admitted in evidence and respectively marked Petitioner's Exhibit 16 and Petitioner's Exhibit 17.)

(Testimony of Winfred T. Wilson.)

These instruments were executed and delivered on account of "my father's wish to make us members of the firm". At the time the deeds of gift were made to my brother and me and from the time the boat was constructed it had been owned in the following shares:— My father, Henry Wilson, owned 15/32nds; A. B. Johnson owned 2/32nds and the C. R. Wilson Estate, Incorporated, owned 15/32nds. On January 6, 1924, my father gave my mother, Mary H. Wilson a 10/32nds interest in the "Oregon". My brother and I each purchased a 1/32nds interest in the "Oregon" from A. B. Johnson for a total consideration of $4,954.72. (The Stipulation of Facts shows that on September 30, 1919, each of Henry A. Wilson, F. A. Wilson and W. T. Wilson acquired a 5/32nds interest in the "Oregon" from Margaret A. Wilson, as trustee in liquidation of the C. R. Wilson Etate, Inc. for a consideration of $19,531.25 from each, or a total consideration for 15/32nds of $125,000.) After the acquisition by my brother and me of the A. B. Johnson interests in the "Oregon", the ownership of that vessel was in the following persons:— Mary H. Wilson, my mother, owned 10/32nds, F. A. Wilson, my brother, owned 11/32nds and I owned 11/32nds. That ownership continued to January 2, 1929, when the three persons named transferred the 32/32nds shares in the "Oregon" to the petitioner corporation as "a contribution without consideration." Since January 2, 1929, petitioner has **[91]** continuously been

(Testimony of Winfred T. Wilson.)
the owner of a hundred percent of the "Oregon" and seventy-five percent of the "Idaho".

(From page 82 to page 94 of the record the testimony relates to values and valuation of the Steamships "Idaho" and "Oregon". While the witness gave opinion evidence as to higher values, he conceded that the valuations by the Board of Tax Appeals in its decision in the proceeding of Henry Wilson et al. v. Commissioner, 16 B. T. A. 1208 had not been appealed but accepted. These valuations on the entire vessels, as of the dates stated, were as follows:—

Steamship "Idaho", March, 1917,
(February 6, 1917) $395,000.00
Steamship "Oregon", January 2, 1917 ..... $385,000.00

These valuations having been adopted in the Memorandum Opinion of the Board in the present proceedings and being accepted by petitioner, recital of the testimony in regard to values are omitted.)

After the "Idaho" and "Oregon" were transferred to petitioner on January 2, 1929, they were operated in the lumber business for about six months when their operations were stopped and they were laid up. The vessels have been laid up, but we have consistently tried to maintain them in a condition where they could be easily and quickly repaired and put into commission, if business opportunities afforded. (On pages 95 to 97 of the record follows testimony as to the probable useful life of the vessels which is omitted because that factor

(Testimony of Winfred T. Wilson.)

is not at issue.) While the vessels have been laid up from [92] year to year we have kept a man on board each of them. He keeps the boat in pretty fair condition and does the painting on it. We usually try to dock the boats and to paint and repair the bottoms once a year to keep the boats in seaworthy condition. (On pages 99 and 100 of the record follows testimony as to requirements and estimates of cost of putting the vessels into commission, which is omitted because immaterial to issues on appeal.)

The two vessels have been constantly retained and maintained by petitioner, even though they have not been operated, because we expected to put them back in commission. It has always been the purpose of the corporation to re-engage in the shipping and lumbering business and the two vessels have always been considered a part of its operating assets.

Petitioner did not declare any dividends during the years 1932, 1933 and 1934 because we did not believe the earnings sufficient, owing to the impaired value of the assets. My brother and I have never abandoned the original idea of operating the company as a logging, milling and shipping company. If we were to enter the logging, lumbering and milling business today, I estimate that it would require fully a million and a half dollars, if not more. When we were operating before the dissolution of our business we had about a million and a half dollars

(Testimony of Winfred T. Wilson.)

in it. Timber lands are not so cheap today and mills and logging equipment are tremendously expensive. We acquired and held the securities which the [93] corporation owns in order to have liquid assets for the time when we would go back into the lumber, logging and milling business. They could quickly be sold and we would have the cash when we wanted to buy anything we wished.

We did not re-enter the business before or during the taxable years involved because losses in the logging business were pretty heavy and in the manufacturing of lumber the saw-mills were taking big losses. It would be unprofitable to go into a business which was losing money.

The witness identified a copy of his income tax return for 1933. I did not return or pay any tax for that year. I have been unable to locate my returns for 1932 and 1934. I paid no tax in 1934 and I paid something like $150.00 in 1932. I helped my brother in checking his income tax returns for each of the years involved. The witness identified copies of the income tax returns of his brother, Francis A. Wilson, for the years 1932 and 1933 and stated that he had seen the return for 1934. The returns of my brother for the years 1932 and 1933 showed no tax returned for either year and to the best of my knowledge the return for 1934 showed no tax. The failure of the corporation to declare dividends during the years 1932, 1933 and 1934 had very little effect upon the individual income upon

(Testimony of Winfred T. Wilson.)

either my brother's individual income or my individual income. The failure to declare dividends did not result from any discussion between my brother and me of possible taxes falling upon either of us individually. [94]

I desire to correct a statement made in my testimony this morning. The amount of money on deposit with the Anglo California Bank as of December 31, 1931, or January 1, 1931, is not shown by the ledger sheets in my possession. At the time I made the corporation return for 1932 the ledger sheet was available and I am absolutely sure that the amount stated in that income tax return as the balance in that bank was correct. Our books were kept on the accrual basis and the items of interest which had accrued during each of the taxable years 1932 and 1933 were correctly reported for each year.

Cross-Examination

June 6, 1939.

The witness identified the petitioner corporations income tax returns for each of the years 1929, 1930 and 1931 which were respectively marked for purposes of identification only as Respondent's Exhibits A, B, and C.

At all the times since incorporation I have been the secretary and treasurer of the corporation and have kept its books. Referring to Exhibits "A", "B" and "C" marked for identification I would say that I think the balance sheets appearing there-

(Testimony of Winfred T. Wilson.)

in were taken from the books of the corporation.

Referring to the opening balance sheet in Respondent's Exhibit "A" for identification I have no recollection concerning a cash item of $200,000., nor the $200,000. notes payable, nor the item under liabilities of common stock $698,000. shown therein, or recall what they are. The $466,000. item represents stock in domestic corporations. I don't recall [95] where those stocks came from.

(On interruption by petitioner's counsel, the witness testified in substance as follows:— I do not have the books of account for the years 1929, 1930 and 1931 in my possession here in court. At no time during the preparation of this case was my attention in any way called to the books of account for those years. On the questions being asked I have not seen the record for many years.)

Cross-Examination
Resumed

I presume our books of account would show what those items represented for the year 1929 when the corporation first started business. As I recall, my brother and I paid a thousand dollars into the corporation for stock and I do not recall having paid any other money. I do not recall what the item of $695,000. on the balance sheet represents; nor the item of cash of $131,173.43 on the closing balance sheet for December 31, 1929, or that such item was represented by I.O.U.'s; nor where the money came

(Testimony of Winfred T. Wilson.)

from to purchase the $486,000. worth of stock shown on the balance sheet at December 31, 1929. I have no information with respect to the note payable item at the end of December 31, 1929, of $200,000. (On being shown the exhibit from which he was being questioned the witness testified.) The $200,000. note payable item went out of the balance sheet on December 31, 1932, and it was in the opening balance sheet for December 31, 1931. I have forgotten what it represented.

The cash shown in the balance sheet of December 31, [96] 1930, on Respondent's Exhibit "C" for identification was $56,593.58, but I do not recall whether it was cash or whether we might have had some I.O.U.'s in the cash box. In preparing the returns we took the figures representing cash from the books and the I.O.U.'s, if we had any, in the cash box. We used I.O.U.'s right along and I do not recall whether the $200,000. in the opening balance sheet was represented by an I.O.U.

As shown by the balance sheet for December 31, 1930, stocks of domestic corporations were purchased increasing the investments up to $504,595. On the liability side of that balance sheet common stock is shown at $800,000., an increase from the opening balance sheet which showed $748,000.

For the year 1931 the balance sheets show an increase from $56,593.58 to $1,642,298.24, a large part of which was represented by I.O.U.'s, but how much I cannot recall. I have no record of the I.O.U.'s in

(Testimony of Winfred T. Wilson.)
our books of account and we have no record of petty cash. I have no ledger sheets in which the I.O.U.'s or petty cash appear. I can balance my books without the record of those items. The balance shows $2,500,000. as common capital stock at December 31, 1931. The books and records of the corporation show the profit and loss from the lumber business for the years 1929 to 1934. I do not recall whether they show a profit or not. "Business was very depressed then; it was awful hard to sell lumber. There was no building going on. It was no criterion of the conditions of the lumber business under normal conditions." [97]

The ledger states the capital account of the corporation as of January 2nd, $2,500,000. The capital account represents the I.O.U.'s and various investments and the boats. The investment in the boats is $75,000. for the "Idaho" and $100,000. for the "Oregon" in the year we formed the corporation. The page of the ledger sheet from which I am reading does not state any specific year but the entry was made in the year which the corporation was formed.

Referring to the entry of capital account, I do not see any stock dividend of $35,000. there. The item "March 30, Transfer from surplus $35,000" represents transfer from surplus and I can make no other explanation. The item "January 31st Transfer from treasury stock, $10,000." represents transfer from the treasury stock and I can make

(Testimony of Winfred T. Wilson.)

no other explanation. The ledger shown me is the ledger for the years 1932, 1933 and 1934. We have another ledger covering the years 1937, 1938 and 1939, but I do not know whether we have a ledger covering the years 1929, 1930 and 1931. (At request of respondent's counsel the ledger identified as covering the years 1932, 1933, and 1934 was ordered marked for identification only as Respondent's Exhibit "D".)

The corporation has a journal which I have here and which covers the years 1932 to 1934. It does not cover the years 1929 to 1932, we kept a journal for that time but I do not know what became of it and doubt whether I would be able to find it. [98]

(Counsel for respondent requested that the books for the years 1929 to 1932 be produced and he advised that in the absence of production he proposed to offer secondary evidence regarding the financial condition of petitioner corporation for that period. Counsel for petitioner explained that he considered that the books of 1929-1932 had nothing to do with the issues and were entirely immaterial, that he had not called upon petitioner to produce accounts for years prior to the years involved. The presiding member of the Board made no order for production but on the day following the books for the years 1929 to 1932 were produced at the hearing.)

The corporation maintains such books and records as it maintains in Los Angeles, in Reno, Nevada, and in San Francisco. The business of the

(Testimony of Winfred T. Wilson.)

corporation is all done in Los Angeles and is conducted in part by myself, my brother and a man in Los Angeles. Our business in Los Angeles is done in the Wilson Building on Wilshire Boulevard and at our lumber yard on Pico Boulevard. We started business in Los Angeles with the corporation when we formed it on December 14, 1928.

We have maintained a bank account in Los Angeles with the Los Angeles branch of the Bank of America. The bank book is in Los Angeles but the bank statements for that account are mailed to us in San Francisco and I have them here.

I kept the books on the accrual basis. Besides the ledger (Respondents Exhibit D for identification) we have various records here, sales books and various records. There [99] was a bank book kept in Los Angeles under my supervision and direction but I do not know whether it was kept under my supervision and direction from 1929 to 1934.

Resumed Hearing

June 7, 1939.

(At this session two witnesses, Albert F. Pillsbury and S. A. Livingston, were called by petitioner to testify as to the value of the Steamship "Idaho" as of February 6, 1917, and the Steamship "Oregon" as of January 10, 1918. As the value of those vessels has been determined by the Board and such valuation is accepted by petitioner, no statement of the testimony of those witnesses is presented.)

(Testimony of Winfred T. Wilson.)

Cross-Examination
of Winfred T. Wilson
Resumed

The stocks of domestic corporations shown in Petitioner's Exhibit 7 were in the possession of the corporation in 1932 and were acquired prior to January 1, 1932, by purchase for cash. The stocks shown on Exhibits 8, 9 and 10 were also purchased for cash. The cash came from the capital of the corporation not out of earnings. In December, 1928, we put in $1,000. That was the beginning of the corporation. Later we put in $685,000. contributed in cash and other assets. Later $50,000. more cash was put in making a balance of $746,000. as of January, 1930. During January, 1930, $54,000. was contributed in cash making a balance of $800,000., January 1, 1931. During 1931 $1,700,000. in I.O.U.'s plus $480,312.24 which we had in the San Francisco Bank was contributed. The $480,000. [100] was contributed by myself and my brother 50-50 during 1931 from the account in the San Francisco Bank belonging to myself and my brother.

After the $480,000. was contributed to capital in 1931, $35,000. was transferred from the book surplus. This amount came from profit and loss into the surplus account and as profit and loss it represented the total operations of the business.

I cannot tell you the amount of interest the corporation received from bonds during the year 1932. We have a record of the total interest received each

(Testimony of Winfred T. Wilson.)

month but it is not itemized. From accounts receivable during the year 1932, my notations show that we got $1,726.41 from Woodhead Lumber Company; $1,324. from the San Francisco Bank in December and $1,312.50 in April; $8.40 and $10.59 from Hutton in January and $7.34 from Hutton in May. The principal source of interest was the Woodhead Lumber Company and the San Francisco Bank.

The interest account for 1933 in our general ledger does not make a break-down of the total interest received for the various items, bonds, accounts receivable and bank accounts. We kept an account of the total interest received each month without segregation. Our bank books would show the interest received from banks. We get the information which we enter in our ledger account from payments made each month—we get a payment from the Woodhead Lumber Company and we get the bank statements of the interest allowed from the bank. I have no [101] itemization here to show whether the Woodhead Lumber Company paid interest in 1935. For the year 1934 and the other years here involved there is some itemization.

I examined the books of the Woodhead Lumber Company. I am not an officer or stockholder of that corporation and have no interest of any kind in it.

I was permitted to examine the corporation's books because it owed us a great deal of money and

(Testimony of Winfred T. Wilson.)

Mr. Woodhead was a friend of mine. We wanted to know if we were going to get our money. It looked pretty bad. So Mr. Woodhead showed us everything he had. I believe I made the examination in 1934.

The Woodhead Lumber Company of Nevada bought the inventory and physical assets of the Woodhead Lumber Company of California in the latter part of 1932 and in consideration gave its note for $25,000. and $37,000. worth of its capital stock. The Woodhead Lumber Company of California was indebted to the petitioner but the Nevada corporation was not, except that we started to sell lumber to it. The Woodhead Lumber Company of California turned over to us as security the note for $25,000. secured by the $37,000. par value stock of the Nevada corporation, but the stock did not have any $37,000. of value. We still sell lumber to the new company.

Cross examination was interrupted and S. A. Livingston was sworn and testified as to valuation of the Steamships "Idaho" and "Oregon". As this testimony is not material to any issue on appeal it is omitted. [102]

Cross-Examination
of W. T. Wilson resumed.

(Here follows testimony on pages 189 to 192 of the record concerning the account of the petitioner corporation with respect to the Steamship "Svea".

(Testimony of Winfred T. Wilson.)

As no issue concerning this account is involved in the appeal, statement of the evidence is omitted.)

Testifying from a document not in evidence but furnished by respondent's counsel, I paid personal income tax deficiency in the amount of $506.09 for 1933 plus a penalty of $25.30 though I reported a net loss for that year. I do not remember whether I paid any personal income tax for the years 1929, 1930 and 1931.

(Testimony concerning the witnesses experience and knowledge regarding sales of vessels or interests in vessels and construction and operation of vessels follows on pages 195 to 204 of the reporter's record. As this cross-examination relates to the witnesses qualification to testify to the value and life of vessels and as no such issue is on appeal, statement of such evidence is omitted.)

Redirect Examination
of Winfred T. Wilson

With regard to the amounts of capital or contributions to the petitioner to which I testified on cross-examination, the usual form of the contributions was in the form of I. O. U.'s. Sometimes we would pay a little on them and sometimes we wouldn't and they are still in the cash box.

I kept the books of account of the corporation dur- [103] ing the years 1929 to 1931 inclusive. Since my testimony given on cross examination yesterday I have found additional books, documents, records

(Testimony of Winfred T. Wilson.)

and papers relating to the financial history of the petitioner during the years 1929 to 1931. (Here the witness identified the ledger for the years 1929, 1930 and 1931.) The ledger is not all complete. The main accounts are here, the profit and loss accounts. The accounts receivable is not complete as to some of the smaller accounts.

(Here follows on pages 206 to 208 of the record testimony relating to the deduction sought in relation to the Steamship "Svea". As this point is not at issue on appeal, no statement of such evidence is given.)

I am not a Certified Public Accountant, have never acted as a bookkeeper other than for petitioner, and have never had any training as a bookkeeper. Whenever I have had any disputes with respect to income tax liability I have hired Certified Public Accountants to put in the facts because I am not able to do it myself.

Explaining my testimony on cross-examination yesterday regarding a $10,000. reduction on the books with respect to treasury stock, we put in that much cash to take it up. No stocks or bonds were transferred to the corporation by my brother and me.

I don't understand the technical meaning of the term "surplus" as compared with the term "paid in surplus" very well, I am not an expert on bookkeeping. [104]

With respect to the Woodhead Company account concerning which I gave testimony this afternoon,

(Testimony of Winfred T. Wilson.)

we never recovered the $5,000. The account was a large account and we recovered only a portion thereof through life insurance which Mr. Woodhead assigned to us to save us from loss of all that money.

(Here follows on pages 210 to 213 of the record testimony relating to value and condition of the Steamships "Idaho" and "Oregon", which, because it does not relate to any issue on appeal, is not reduced to statement.)

Recross-Examination
of Winfred T. Wilson

On direct examination I testified that a receiver had been appointed for the Kentucky Fuel and Gas Corporation, I think it went into receivership in 1931, but I am not sure. In my investigation I looked up quotations on the 6½ bonds of the corporation. We claimed partial deduction on those bonds for 1934. I looked up the market quotations of the bonds in 1932 but do not recall the sale or bid and asked prices with respect to them. I think the charge-off was a general one against the bonds we owned. I have the book of account where the charge-off of Kentucky Fuel and Gas bonds was made. The book shows that we acquired the bonds December 1st but does not give the year. I do not know from whom we acquired the bonds of a face value of $15,000. in 1932.

THOMAS MURPHY

was called as a witness by and on behalf of the petitioner and [105] having been first duly sworn testified on June 7, 1939, in substance as follows:

Direct Examination

I am a Certified Public Accountant employed by Barrow, Wade, Guthrie & Co., a firm of national and international accountants, as a senior accountant. The nature of my work as a senior accountant covers the general field of auditing, cost accounting and Federal and State income taxation. I am admitted to practice before the Treasury Department and the Board of Tax Appeals.

In my capacity as an employee of Barrow, Wade, Guthrie & Co. I have made an examination of the books of petitioner. My firm was employed to make that examination by Judge Graupner, counsel for petitioner, subject to the approval of Francis A. Wilson, an officer of the corporation, in August of 1938. My instructions were given by Judge Graupner. He stated that he wished to have an impartial examination made of the books and records and all other papers which would be made subject to my inspection and from those records to prepare balance sheets for the years ended December 31, 1932, and annually thereafter to include December 31, 1934, to reflect in the amended statements all adjustments of errors which I located in the course of my examination, including particularly those errors of principle which I discovered. Also, I was to make a survey of income and earned surplus accounts and

(Testimony of Thomas Murphy.)

to make such adjustments in those accounts as I found necessary. [106]

I was advised that the purpose of the examination and my report was for use in relation to petitioner's income tax disputes for the years 1932 to 1934 inclusive. Also, I was told it was desired to have a report which would provide the basis for more complete accounting for the years thereafter. This report was completed by my firm and submitted to the client. When it became apparent that this case was to go to trial I made additional examinations of several matters and prepared additional schedules and made slight adjustments in two schedules so as to make the facts more informative.

In the preparation of the report the scope of my examination did not go so far as to be a detailed one, but I was to make an analysis of all of the balance sheet accounts and to make due adjustments for any errors that I located in the course of my examination. I was also to make a survey of all of the income accounts for the years 1929 to 1934 inclusive so as to properly state the earned surplus account at each of the balance sheet dates included in the period of examination.

The books that were made available to me were the general ledger, journal and the lumber sales sheets for the years 1932 to 1934 inclusive. Also, I saw the minute book and the capital stock record book, but I found no other evidence of any other records or books of account than those which I have detailed. In my opinion, those books were kept on

(Testimony of Thomas Murphy.)

the accrual basis with the possible exception in respect of dividends on the stocks of domestic corporations. This diversion of [107] treatment of dividends is somewhat common and is apt to occur in accounting.

As to items of income and deduction, the books and returns were in accord each with the other. I attempted but was unable to take a trial balance from the general ledger as of January 1, 1932, December 31, 1932, December 31, 1933, and December 31, 1934, because the general ledger accounts, as submitted to me, lacked certain other accounts necessary to establish a complete balance of the records. From information furnished me by Francis A. Wilson, one of the officers of the corporation, I was able to complete a balance of the books for all four dates named. I went further than that: I compared the completed trial balance, with the reconcilement items, with the returns filed for the three years and found that in each case a combination of the individual items found in the general ledger would tie in with the classification appearing in the balance sheets in the returns. (The witness then identified three sheets of typewritten paper as being general ledger trial balances for the three years "before reconciliation.") The information from these sheets was taken from the books of the company. No year dates were available but the information was supplied by officers of the corporation. Because I ultimately was able to reconcile the figures through the

(Testimony of Thomas Murphy.)

additional information supplied and to tie them into the Federal tax returns for those years, it is my opinion that these trial balances are correct, even though there may be [108] deficient information contained in the books. The three sheets of paper fastened together were offered in evidence for the purpose of showing what the books of petitioner show for the periods indicated and were submitted and marked Petitioner's Exhibit No. 18.

I made certain reconciliations with respect to the general ledger trial balance for the purpose of indicating specifically the particular items which were omitted. There was no ledger sheet in the books of the taxpayer to evidence the account of the Anglo-California National Bank which showed a balance of $4,694.28 on January 1, 1932. I verified that item by examining the cancelled bank book that was issued by the bank to evidence that account. I also have seen the account of the Atlantic Lumber Company showing the balance due the taxpayer on January 1, 1932, in the sum of $45.00. That account will be found in the ledger that was presented as evidence this morning by Mr. Wilson. Other than that I have not seen any of the accounts which I have attempted to reconcile as shown by the schedule of reconciliations which I prepared, and hold in my hand and I have never seen ledger sheets to substantiate them, but have been given explanations by officers of the company as to what they consisted. When I say "other than that I have not seen the

(Testimony of Thomas Murphy.)

accounts", I refer to the cash item which is shown for the first three years in excess of one million dollars and at December 31, 1934, of 898,000 odd dollars. It was explained to me that those items were represented by I. O. U.'s which were placed in the cash drawer of Wilson Brothers [109] & Company and that it was necessary to take into account those I. O. U.'s in effecting a balance of the general ledger. I had not seen any of those I. O. U.'s at the time of preparing the statement of reconciliation. I have not seen any of the I. O. U.'s which would induce the particular amounts but I have seen one that is currently being carried in the cash box of the taxpayer. It is for $843,438.54, consisting of two equal parts, one of which is purportedly due by Francis A. Wilson and the remainder owing by Winfred T. Wilson. (Petitioner offered in evidence the schedule or statement of reconciliation concerning which the witness testified as Petitioner's Exhibit No. 19 and the objection to admission thereof by Respondent's counsel was sustained by the presiding Member.)

The attention of the witness was called to Petitioner's Exhibit No. 6, entitled "Wilson Bros. and Co. Cash in banks," showing total cash in banks as follows:

January 1,	December 31,		
1932	1932	1933	1934
$408,999.65	$96,638.23	$9,186.43	$73,707.36

(Testimony of Thomas Murphy.)

I prepared the original of this exhibit. I determined the cash in banks as of the various dates shown from examining the ledger sheets of the company and comparing them with the ledger sheets in possession of the listed banks, bank statements or bank pass books. There was no additional amount of cash shown by the books of the company.

The attention of the witness was called to Petitioner's Exhibit No. 3. (Corporation Income Tax Return of petitioner for [110] calendar year 1932.) I attempted to reconcile the cash shown on the return as $1,642,298.24 as of January 1, 1932, with the cash for that date shown on Exhibit 6 as $408,999.65, but I could locate no additional cash either in the form of cash, currency or bank deposits. The attention of the witness was called to Petitioner's Exhibit No. 4 (Corporation Income Tax Return of petitioner for calendar year 1933). The exhibit shows cash at the beginning of the taxable year as $1,106,-377.07 and I could not reconcile the difference between that amount and the $96,638.23 shown on Exhibit 6 for the same date. I could locate no further deposits or other forms of cash. At the end of the year 1933 cash in Petitioner's Exhibit No. 4 is shown to be $1,022,123.45. I could not reconcile this figure with the $9,186.43 shown in Exhibit No. 6 for the same date for the reasons given before. In Petitioner's Exhibit No. 5 (Corporation Income Tax Return of Petitioner for calendar year 1934) cash at the end of the year 1934 is shown as $972,147.49.

(Testimony of Thomas Murphy.)

I could not reconcile that figure with the $73,707.36 shown in Exhibit No. 6 for the same reasons.

I have examined the books of petitioner but did not encounter any item or sheet relating to $200,000. of notes payable.

The witness identified a paper as being a statement of accounts receivable of the petitioner as of January 1, 1932. The items on that paper, with the exception of the accounts of Fisher Company $35. and E. F. Hutton & Company $5,173.99 were [111] taken from the ledger of the company which are here in the court room. With the exception of the items relating to Fisher Company and E. F. Hutton & Company the statement was admitted in evidence and marked Petitioner's Exhibit No. 19. (As admitted, Exhibit No. 19 shows accounts receivable as of January 1, 1932, to be $62,107.06.)

The witness identified a paper as being a statement of the accounts receivable of the petitioner as at December 31, 1932. The statement shows all the accounts receivable of petitioner that are set forth in the books of account. Also, it shows an account in the name of J. C. Smith Lumber Company in the sum of $87.89 which is not disclosed in the ledger sheets. With the exception of the item $87.89 under the name J. C. Smith Lumber Company, the statement was admitted in evidence and marked Petitioner's Exhibit No. 20. (As admitted Exhibit No. 20 shows accounts receivable as of December 31, 1932, to be $72,574.58.)

(Testimony of Thomas Murphy.)

The witness identified a paper as being a list of the accounts receivable of petitioner as at December 31, 1933. The list was compiled from the books of account of the company present in the court room—with the exception of the item Advance Lumber Company $100. With the exception of the item of $100. as to Advance Lumber Company, the list was admitted in evidence and marked as Petitioner's Exhibit No. 21. (As admitted Exhibit No. 21 shows accounts receivable as of December 31, 1933, to be $94,824.91.) [112]

The witness identified a paper as the schedule of accounts receivable of petitioner as of December 31, 1934. That schedule is complete from the books of account of the company without exception. I discovered accounts receivable with respect to the shareholders and officers of petitioner but did not list them on this schedule. I classified them separately on the balance sheet which I prepared for the information they may contain in this proceeding. This schedule, together with the three exhibits immediately preceding, indicate only those accounts receivable which had to do with the company's trade in business, namely: the sale of lumber and the accounts representing advancements in respect to the Steamship "Svea". The schedule was admitted in evidence and marked Petitioner's Exhibit No. 22. (Exhibit No. 22 shows total accounts receivable as of December 31, 1934, to be $103,002.60).

The witness identified a paper as being an anlysis

(Testimony of Thomas Murphy.)

of the ledger sheet appearing in Petitioner's books of account present in the courtroom. The analysis concerns the account of petitioner carried with F. A. Wilson for the period April 26, 1933, to January 2, 1935, inclusive. The dates and amounts are shown on the ledger sheet of that account but the explanations in the schedule are taken from journal entries and other ledger entries which show that Mr. Wilson, as a stock broker, bought and sold securities for which he was accountable to petitioner. The schedule was admitted in evidence and [113] marked Petitioner's Exhibit No. 23.

In my opinion as an expert accountant petitioner, during the years 1933 and 1934, kept its accounts on the direct write-off method with respect to bad debts and the books so reflect. The account entitled "Reserve for Bad Debts" which appears in the books of the corporation is not unusual. Corporations frequently set up a "Reserve for Bad Debts" in which there is provision made for debts known or believed to be bad, and such reserve is a balance sheet item and operates to reduce the carrying value of the asset related to it. The reserve for bad debts expression may be used in two entirely different senses, and it is my opinion that in this case the term is used as a valuation balance sheet account and does not show by which means it elected to take off deductions for bad debts from a tax point of view. It is my opinion that the petitioner is on a direct write-off basis under the Revenue Act, irrespective

(Testimony of Thomas Murphy.)
of the fact that for accounting purposes it carried a reserve for bad debts.

(Here follows testimony on pages 265 to 269 of the reporter's record and the admission of Petitioner's Exhibits Nos. 24 and 25 relating to maintenance expenses of the Steamships "Idaho" and "Oregon" and the accounts receivable of the Steamship "Svea". As these items are not at issue on appeal no statement of the testimony in relation thereto is included. Following such testimony on pages 269 and 270 of the record the witness further testified to his examination [114] relating to the bank interest accounts of petitioner. As this item is not at issue on appeal the testimony relating thereto is omitted.)

In connection with the reserve for bad debts, with exception of the provision for uncollectibility of the Steamship "Svea" account, immediately, or at least as of the same date, which was December 31 of the years involved, the entry setting up the provision for bad debts was followed immediately by a charge back to reserve for bad debts account and a credit to the related assets account. That applies with respect to the Kentucky Gas bonds and the Woodhead Lumber Company.

For the year 1933 there were nine specific accounts receivable which were credited, thereby eliminating the accounts as assets from the books of the corporation, but leaving the Steamship "Svea" provision in the reserve for bad debts. In the year 1934

(Testimony of Thomas Murphy.)

the two credits to asset accounts with corresponding charges to the reserve for bad debts were with respect to the Kentucky Fuel & Gas Corporation bonds and the Woodhead Lumber Company in respective amounts of $5,500. and $5,000.

(Here follows testimony on pages 272 and 273 of the reporter's record relating to interest on bank deposits which, because not material to issue on appeal, is omitted.)

Referring to Petitioner's Exhibit No. 7 (Stocks of Domestic Corporations as of January 1, 1932.) I prepared the schedule. The figures under the heading "Number of Shares" [115] were taken from the ledger sheets carried individually for each investment of petitioner. The information as to the names of the corporations were taken from the same source and also the figures shown under "Cost". The figures for "Approximate Market Value" were taken from bank and quotation records. The figure I used in each case was the exact amount of the last sale and, if there did not happen to be a last sale, I took the bid price. However, there were two exceptions. With respect to the Anglo National Corporation I went to the office of the San Francisco Stock Exchange where the stock was listed and secured from its official records the price at which the last sale occurred. In connection with the Weeden & Co. stock I communicated with an officer of that corporation and was given orally a price at which sales had been negotiated through that company for shares of its

(Testimony of Thomas Murphy.)

own stock about the time of the balance sheet date. The same explanation applies with equal force to Exhibits 8, 9 and 10. (Petitioner's Exhibits Nos. 8, 9 and 10 are schedules of "Stock of Domestic Corporations" as of December 31, 1932, 1933 and 1934 respectively.) There is an exception to Exhibit No. 10 wherein the last item on the schedule is labeled "Unidentified difference" and opposite that item under "Approximate Market Value" there is the word "none", indicating no value whatever. Under the word "Cost" are the red ink figures of $212.50 indicating a deduction from the other assets to come to a net balance which would be $212.50 less than the aggregate cost as shown by the [116] Exhibit. There is simply no way of explaining this difference. Petitioner's ledger accounts are thus $212.50 greater than the amount appearing in the Federal income tax return.

There is another exception involving $250,000. The petitioner's book shows two ledger accounts entitled "Treasury Stock" and that $250,000. did not represent actual value in the form of treasury stock. As shown by the capital stock records, there never had been any capital stock issued in excess of $1,000. par value. I could find no records to indicate any repurchase or other acquisition of any stock of the corporation, therefore, I eliminated the $250,000. as being of no value whatever.

Referring to Petitioner's Exhibit No. 11 (schedule of "Bonds of Domestic Corporations"), I prepared this statement. The cost figures for the

(Testimony of Thomas Murphy.)

four dates (January 1, 1932, and December 31 for each of the years 1932, 1933 and 1934) are taken from the ledger accounts and are in agreement. The cost figures for Kentucky Fuel Gas Corp. bonds as shown by Exhibit 11 are as follows:

$18,000.	1st lien s. f. 6½% A bonds due 1942, at January 1, 1932	$9,000.00
15,000.	1st lien s. f. 6½% A bonds due 1942, at December 31st, 1932	450.00
10,000.	1st lien s. f. 6½% A bonds due 1942, at December 31, 1933	20.00
$43,000.	total par value of said bonds had a cost on December 31, 1933, of	$9,470.00

I made an investigation upon which I could base an opinion as to whether or not there was any loss in value of the bonds of the Kentucky Fuel & Gas Corporation. I have here [117] information which I acquired with respect to those bonds. In the first place, due to the rapid shrinkage of the market value of those bonds, it was evident that a substantial loss of value had occurred from one of two reasons: First, a mere fluctuation in market conditions which might be due to extrinsic factors and also it might represent a final and permanent loss of value within the bond itself. That would be particularly true because these bonds were a senior issue; they had sinking fund provision; they carried a fairly high coupon and yet sold as low as $2. per hundred dollar bonds therefore, I considered market value would have a very considerable bearing on evidence of worth or lack of it.

(Testimony of Thomas Murphy.)

The source of my information as to these market values is the Bank and Quotation Record and as to the first sinking fund 6½ bonds of 1942, I will give the bid and ask prices in that order and each quotation will be on the basis of a $100. bond:

January 1, 1930	$74.00 and $79.00
December 31, 1930	$35.00 and $45.00
December 31, 1931	$ 5.00 and $ 7.00
December 31, 1932	$ 1.25 and $ 4.00
December 31, 1933	$ 2.00 and $ 4.00
December 31, 1934	$ 4.50 and $ 6.00

For the years 1935 and thereafter for the dates given I will state only the bid price: December 31, 1935, $8.00; December 31, 1936, $18.50; November 30, 1937, $8.00.

Assuming for the moment that the deduction of $5,500. claimed with respect to Kentucky Fuel & Gas Corporation bonds might not be allowed for some technical reason, it is my opinion that from an accounting point of view as distinguished from a [118] tax point of view there should be provision to reduce the book value and the carrying value of these bonds to at least as low a figure as appears in the accounts of this corporation. I think that the provision of $5,500. is certainly not greater than would be made under good accounting practice in a financial statement of the company.

(Testimony of Thomas Murphy.)

Cross-Examination
of Thomas Murphy

With respect to Kentucky Fuel & Gas Corporation debentures 6½s of 1938 the bid and ask prices from 1930 to 1934 were respectively as follows:

January 1, 1930	$73.00 and $77.00
December 31, 1930	$45.00 and $55.00
December 31, 1931	$ 1.25 and $ 1.50
December 31, 1932	none and $ 2.00
December 31, 1933	none and $ 2.00
December 31, 1934	none and $ 2.00

Whereupon, the petitioner rested and respondent offered documents marked for identification as Respondent's Exhibits "A", "B" and "C" (Petitioner's income tax return for the years 1929, 1930 and 1931 respectively) in evidence. Over objection by petitioner and on exception the documents were admitted in evidence as Respondent's Exhibits "A", "B" and "C".

The foregoing evidence together with the Stipulation of Facts filed with the United States Board of Tax Appeals on June 6, 1939, and the Exhibits referred to in the foregoing statement constitute all of the material evidence adduced at the hearing before said Board and relating to the issue involved [119] in the petition for review of the decision of said Board.

The deficiency notices attached to the petitions on file in the above-entitled and numbered proceedings and designated in the foregoing statement as Petitioner's Exhibits numbered 1 and 2 are to be considered as before the court without additional transcript thereof for the record on appeal.

There are to be attached hereto and made a part hereof on transmission of the record from the Clerk of the United States Board of Tax Appeals to the Clerk of the United States Circuit Court of Appeals, Ninth Circuit, the following Exhibits offered by the parties to the proceedings and admitted in evidence, viz:

Petitioner's Exhibit

3—Petitioner's income tax return for 1932
4—Petitioner's income tax return for 1933
5—Petitioner's income tax return for 1934
6—Statement of Petitioner's cash in banks
7—Statement of Petitioner's stock ownership 1/1/32
8—Statement of Petitioner's stock ownership 12/31/32
9—Statement of Petitioner's stock ownership 12/31/33
10—Statement of Petitioner's stock ownership 12/31/33
11—Statement of Petitioner's bond ownership
18—(3 Sheets) Petitioner's General Ledger Trial Balances (after closing) 1932-1934
19—Petitioner's accounts receivable 1/1/32
20—Petitioner's accounts receivable 12/31/32
21—Petitioner's accounts receivable 12/31/33
22—Petitioner's accounts receivable 12/31/34 [120]
23—Analysis petitioner's accounts receivable from F. A. Wilson

Respondent's Exhibit

A—Petitioner's income tax return for 1929
B—Petitioner's income tax return for 1930
C—Petitioner's income tax return for 1931

The foregoing Revised Statement of the Evidence is approved by the undersigned as attorneys for the petitioner and respondent on review.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for Petitioner
on Review
J. P. WENCHEL
Counsel for Respondent
on Review. [121]

PETITIONER'S EXHIBIT No. 3

Computation proved

0-12

Page 1 of Return

Form 1120
TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE
(Auditor's Stamp)

CORPORATION INCOME TAX RETURN
For Calendar Year 1932

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1933

File Code 781
Serial Number 856828
District 1-Calif.
(Collector's Stamp)

RECEIVED MAR 31 1933 COLLECTOR INT. REV. SAN FRANCISCO, CALIF.

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

WILSON BROS. & CO.
(Name)
1312 Russ Building.
(Street and number)
San Francisco, Calif.
(Post office and State)

It is Essential, Except Where Otherwise Provided in the Instructions, That This Form be Completely Filled Out Irrespective of any Statements, Schedules, or Reports Submitted Herewith

Date of Incorporation December 4, 1928

Under the Laws of what State or Country Nevada

The Corporation's Books are in Care of _____ Located at _____

Kind of Business Lumber & Steamship In This Consolidated Return of Two or More Corporations? No

ATTACH REMITTANCE HERE

Item and Schedule No.			
	GROSS INCOME		
1.	Gross Sales (where inventories are an income-determining factor), $ _____ ; Less Returns and Allowances, $ _____ ; Net Sales		28 725 96
2.	Less Cost of Goods Sold:		
	(a) Inventory at beginning of year	20 942 18	
	(b) Material or merchandise bought for manufacture or sale	12 413 55	
	(c) Miscellaneous costs (From Schedule A, Column D): (1) Salaries and wages, $ _____ ; (2) Other costs, $ _____ ; Total		
	(d) Total of lines (a), (b), and (c)	33 355 73	
	(e) Less inventory at end of year		33 355 73
3.	Gross Profit from Sales (Item 1 minus Item 2) (LOSS)		4 629 77
4.	Gross Receipts (where inventories are not an income-determining factor)		
5.	Less cost of operations (From Schedule A, Column D): (a) Salaries and wages, $ _____ ; (b) Other costs, $ _____ ; Total		
6.	Gross Profit where inventories are not an income-determining factor (Item 4 minus Item 5)		
7.	Interest on Loans, Notes, Mortgages, Bonds, Bank Deposits, etc.		18 949 59
8.	Rents		795
9.	Royalties		
10.	Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)		5 193 76
11.	Dividends on:		
	(a) Stock of Domestic Corporations subject to taxation under Title I of Revenue Act of 1932		
	(b) Stock of Domestic Corporations not subject to taxation under Title I of Revenue Act of 1932		18 258
	(c) Stock of Foreign Corporations		
12.	Other Income (State nature of income): INC. ... REV ACT 1932. ASSESSMENT		
	(a) _____		
	(b) _____ Tax ... $ 4243.36		
13.	TOTAL INCOME IN ITEMS 3, AND 6 TO 12, INCLUSIVE 5% = 567.17		53648 97
	DEDUCTIONS		
14.	Compensation of Officers (From Schedule C)		None
15.	Rent on Business Property		1 416 80
16.	Repairs (From Schedule D); Salaries and Wages, $ _____ ; Other Costs, $ _____ Total		
17.	Interest		
18.	Taxes (From Schedule E)		752 28
19.	Losses (From Schedule F) Steamship Operations		4 547 06
20.	Bad Debts (From Schedule G)		
21.	Dividends (From Schedule H)		18 258
22.	Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)		11 180
23.	Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 23)		
24.	Other Deductions Not Reported Above (Explain below, or on separate sheet):		
	(a) Salaries and wages. (Not included in Items 2, 5, 14, or 16 above)		5 780
	(b) General Expense		2 405 83
	(c)		
	(d)		
25.	TOTAL DEDUCTIONS IN ITEMS 14 TO 24		44 396 82
26.	NET INCOME (Item 13 minus Item 25)		13 760 92
27.	Less: NET LOSS FOR 1931 (Submit schedule)	LOSS	
28.	NET INCOME FOR TAX COMPUTATION (Item 26 minus Item 27)		

U. S. BOARD OF TAX APPEALS
DOCKET NO. 83297
JUN - 6 1936
PETITIONER'S EXHIBIT 3
RESPONDENT'S

COMPUTATION OF TAX

29.	Net Income (Item 28 above)	
30.	Income Tax (13½% of Item 29) (or 14½% of Item 29, if this is a consolidated return)	
31.	Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)	
32.	Income Tax Paid to a Foreign Country or United States possession by a domestic corporation (See Instruction 30)	
33.	Balance of Tax (Item 30 minus Items 31 and 32)	

An amended return must be marked "Amended" at top of report. Checks and drafts will be accepted only if payable at par.

6-12

SCHEDULE E—BALANCE SHEETS (See Instruction 6f)

Item	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1. Cash		$ 1 642 298 24		$ 1 106 377 07
2. Notes receivable				14 000
3. Accounts receivable	$ 102 166 33		$ 211 628 86	
Less reserve for bad debts		102 166 33		211 628 86
4. Inventories:				
Raw materials	$		$	
Work-in-process	20 942 18			
Finished goods				
Supplies				
		20 942 18		
5. Investments (nontaxable):				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Other investments:				
Stocks of domestic corporations	$ 766 670		$ 1 000 943 50	
Bonds of domestic corporations	12 975		13 425	
Stocks and bonds of foreign corporations				
All other investments or loans	131 250	910 895	122 500	1 136 868 50
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
All other				
8. Capital assets:				
Land	$ 30 000			30 000
Buildings	20 000		$ 20 000	
Machinery and equipment	7 750 50		7 750 50	
Furniture and fixtures	5 000		5 000	
Delivery equipment				
	$ 32 750 50		$ 32 750 50	
Less reserves for depreciation (except on land)	6 850 50	25 900	9 250 50	23 500 00
9. Patents				
10. Good will				
11. Other assets (describe fully):	$		$	
12. TOTAL ASSETS		$ 2 732 201 75		$ 2 522 374 43
LIABILITIES				
13. Notes payable (less than one year)		$ 200 000		$
14. Accounts payable		19 409 11		3 064 68
15. Bonds and notes (not secured by mortgage)				
16. Mortgages (including bonds and notes so secured)				
17. Accrued expenses:				
Interest	$		$	
Taxes				
All other				
18. Other liabilities (describe fully):	$		$	
19. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)	2 500 000			2 500 000
20. Surplus	$		$	
21. Undivided profits		12 792 64		12 309 75
22. TOTAL LIABILITIES		$ 2 732 201 75		$ 2 522 374 43

Remarks: Declared Value 2,500,000.00 (represented by 20 shares)

E-2

6-13

SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 28, page 1 of the return	1033			11	749	81	9. Unallowable deductions:					
2. Nontaxable income:							(a) Pensions, gratuities, and insurance					
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia							(b) Income and profits taxes paid to the United States, and such taxes paid to its possessions or foreign countries if claimed as a credit in Item 32, page 1 of the return					
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended							(c) Federal taxes paid or borne assessed locally					
(c) Interest on obligations of the United States or its possessions							(d) Special assessments taxes tending to increase the value of the property assessed					
(d) Dividends (allowable under Section 26 (p) of the Revenue Act of 1926)				18	258		(e) Purchase and fixtures, additions, or betterments treated as expenses on the books					
(e) Proceeds of life insurance policies paid upon the death of the insured							(f) Reimbursements and proceeds					
(f) Other items of nontaxable income (to be detailed):							(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary					
(1)							(h) Interest on indebtedness incurred or continued to purchase or carry obligations or shares the interest upon which is wholly exempt from taxation					
(2)							(i) Additions to reserves for bad debts which are not included in Item 25, page 1 of return					
(3)							(j) Additions to reserves for contingencies, etc. (to be detailed):					
3. Charges against reserves for bad debts, if Item 25, page 1 of return, is not an addition to a reserve							(1)					
4. Charges against reserves for contingencies, etc. (to be detailed):							(2)					
(a)							(3)					
(b)							(k) Other unallowable deductions (to be detailed):					
(c)							(1)					
5. Total of Lines 1 to 4, inclusive				6	517	11	(2)					
6. Total from Line 14							(3)					
7. Net profit for year, as shown by books, before any adjustments are made thereon (Line 5 minus Line 6)							10. Total of Line 10					
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year				12	792	64	11. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):					
9. Other credits to surplus (to be detailed):							(a) Date paid, Character					
(a)							(b) Date paid, Character					
(b)							(c) Date paid, Character					
(c)							(d) Date paid, Character					
10. Total of Lines 7 to 9, inclusive							12. Other debits to surplus (to be detailed):					
11. Total from Line 17							(a)					
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)				19	309	75	(b)					
							(c)					
							13. Total of Lines 11 and 12					

NET INCOME OR DEFICIT REPORTED IN RETURN FOR 1931 BEFORE DEDUCTING NET LOSS FOR PRIOR YEAR

1. Enter amount of net income or deficit for 1931 before deducting net loss for 1929–1930 ..... $ _____

2. Enter amount deducted in return for 1931 as net loss for 1929–1930 ..... $ _____

KIND OF BUSINESS

3. State the main business engaged in, also whether acting as principal or as agent on commission; state if inactive or in liquidation:

Chart

Chart the proper block below to indicate the general industrial division in which the corporation's main income-producing business falls:

- ☐ Agriculture and related industries, including fishing, forestry, ice harvesting, etc.; also leasing of such property.
- ☐ Mining and quarrying, including gas and oil wells; also leasing of such property.

Manufacturing—

- ☐ Food products, beverages, and tobacco.
- ☐ Textiles and textile products.
- ☐ Leather and leather products.
- ☐ Rubber and related products.
- ☐ Lumber and wood products, including fiber furniture.
- ☐ Paper, pulp and products.
- ☒ Printing, publishing, and allied businesses.
- ☐ Chemicals and allied products, including petroleum products.
- ☐ Stone, clay, and glass products.
- ☐ Metal and metal products, including precious metals and products.
- ☐ Other manufacturing.

- ☐ Construction—excavations, buildings, bridges, railroads, ships, etc.; also equipping and installing operating systems, devices, or machinery without their manufacture.
- ☐ Transportation—rail, water, aerial, motor, etc.; also leasing of such facilities.
- ☐ Public utilities—electric light or power, gas (artificial or natural), pipe lines, telephone, telegraph or radio, waterworks, heating, toll bridges, etc.; also leasing of such utilities.
- ☐ Storage—cold storage, grain elevators, warehouses, safe deposit vaults, etc.; also leasing of such property.
- ☐ Trading—wholesale, retail, or commission.
- ☐ Service—professional, business, amusement, etc.; domestic, including hotels, restaurants, laundries, etc.
- ☐ Finance—banks and other financial organizations, insurance, real estate; also brokers and agents.

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 6

4. Is this a consolidated return of two or more corporations? _____ If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed on a part of this return. See Section 141 of the Revenue Act of 1932 and Instruction 6.

5. Was the income of this corporation included in a consolidated return for the prior year? _____

If so, give name of corporation which filed the consolidated return. _____

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? YES Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? _____ If answer is "yes," give name and address of such predecessor business, and the date of the change in entity. _____

Upon such change were any asset values increased or decreased? _____

If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of actual receipts and disbursements? YES

If not, describe fully what other basis or method was used in computing net income. _____

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock. _____

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

E-3

Schedule A

1. Cost of sales (where inventories are an income-determining factor)

[Not filled in]

2. Cost of operations (where inventories are not an income-determining factor)

[Not filled in]

Schedule B

Profit From Sale of Real Estate, Stocks, Bonds, Etc.

[Not filled in]

Schedule C—Compensation of Officers

[Not filled in]

Schedule D—Cost of Repairs

[Not filled in]

Schedule E—Taxes Paid

[Not filled in]

Schedule F—Explanation of Losses by Fire, Storm, Etc.

[Not filled in]

Schedule G—Bad Debts

[Not filled in]

Schedule H—Dividends Deductible

[Not filled in]

Schedule I—Explanation of Deduction for Depreciation

1. Kind of Property	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquisition	5. Cost	6. March 1, 1913, Value if Acquired Prior to That Date	7. Depreciation Allowed (or Allowable) in Prior Years	8. Depreciation Allowable This Year
Wooden Bldgs.	Jan. 2, 1929		20 Years	$ 20,000.	$	$1000.	$1000.
" Steamers	do	10 Years	20 "	175,000		8750.	8750.
Furniture & Fixs.	"		10 "	5,000		500.	500.
Autos		New		8,249.25		900.	900.
						11150—	11150—

AFFIDAVIT

We, the undersiged, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1932 and the Regulations issued thereunder.

F. A. WILSON

President.

W. T. WILSON

[Corporate Seal] Treasurer.

Sworn to and subscribed before me this 31 day of March, 1933.

W. J. O'CONNOR,

[Notarial Seal] Dep. Coll. [125]

CONSENT FIXING PERIOD OF LIMITATION UPON ASSESSMENT OF INCOME AND PROFITS TAX

IT:E:Aj
RLT-25579

....., 193

In pursuance of the provisions of existing Internal Revenue Laws Wilson Brothers and Company, a taxpayer of San Francisco, California, and the Commissioner of Internal Revenue hereby consent and agree as follows:

That the amount of any income, excess-profits, or war-profits taxes due under any return (or returns) made by or on behalf of the above-named taxpayer for the taxable year (or years) 1932, under existing acts, or under prior revenue acts, may be assessed at any time on or before Dec. 30, 1935, except that, if a notice of a deficiency in tax is sent to said taxpayer by registered mail on or before said date, then the time for making any assessment as aforesaid shall be extended beyond the said date by the number of days during which the Commissioner is prohibited from making an assessment and for sixty days thereafter.

WILSON BROS. & CO.
Taxpayer.

[Seal*] By F. A. WILSON,
Pres.

GUY T. HELVERING
Commissioner of Internal Revenue.
By C C D 5/2/35.
(Date)

*If this consent is executed on behalf of a corporation, it shall be signed with the corporate name, followed by the signature and title of such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which the seal, if any, of the corporation must be affixed. Where the corporation has no seal, the consent must be accompanied by a certified copy

of the resolution passed by the board of directors, giving the officer authority to sign the consent. [126]
RLT/REK-2

Mailed
May -4 1935

IT:E:Aj
RLT-25579
Mr. L. L. Pryor,
155 Sansome Street,
San Francisco, California.

In re: Wilson Brothers and Company,
1312 Russ Building,
San Francisco, California.

Sir:

Receipt is acknowledged of your letter dated April 24, 1935, and the consent transmitted therewith, extending the period of limitation for assessment of income tax on the return of the above-named taxpayer for the year 1932 to December 30, 1935.

The consent has been accepted by the Commissioner. In this connection it is desired to assure you that it is our purpose to proceed to a final determination of the tax liability as expeditiously as possible, and your cooperation to that end will be appreciated.

Respectfully,
CHAS. T. RUSSELL,
Deputy Commissioner.
By (Signed) J. W. CARTER
Chief of Section.

RLT/CCM-2

[127]

CONSENT FIXING PERIOD OF LIMITATION UPON ASSESSMENT OF INCOME AND PROFITS TAX

IT:E:Aj
RLT-25579

Jan. 31, 1935

In pursuance of the provisions of existing Internal Revenue Laws Wilson Brothers and Company, a taxpayer of 1312 Russ Building, San Francisco, California, and the Commissioner of Internal Revenue hereby consent and agree as follows:

That the amount of any income, excess-profits, or war-profits taxes due under any return (or returns) made by or on behalf of the above-named taxpayer for the taxable year (or years) 1932 under existing acts, or under prior revenue acts, may be assessed at any time on or before June 30, 1935, except that, if a notice of a deficiency in tax is sent to said taxpayer by registered mail on or before said date, then the time for making any assessment as aforesaid shall be extended beyond the said date by the number of days during which the Commissioner is prohibited from making an assessment and for sixty days thereafter.

WILSON BROS. & CO.
Taxpayer.

[Seal*] By F. A. WILSON,
President.

GUY T. HELVERING
Commissioner of Internal Revenue.
By C C D 3/1/35.
(Date)

*If this consent is executed on behalf of a corporation, it shall be signed with the corporate name, followed by the signature and title of such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which the seal, if any, of the corporation must be affixed. Where the corporation has no seal, the consent must be accompanied by a certified copy of the resolution passed by the board of directors, giving the officer authority to sign the consent.
RLT/AA3

[Endorsed]: Petitioner's Exhibit No. 3. Admitted in evidence June 6, 1939. [128]

EXHIBIT 4

PETITIONER'S EXHIBIT No. 4

Form 1120
TREASURY DEPARTMENT
Internal Revenue Service
(Collector's Stamp)

CORPORATION INCOME AND EXCESS-PROFITS TAX RETURN
For Calendar Year 1933

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1934

Page 1 of Return

File No. 781

Serial Number 855843

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

WILSON BROS. & CO.
(Name)
1512 RUSS BUILDING,
(Street and number)
SAN FRANCISCO, CALIF.
(Post office and State)

(Collector's Stamp)
MAR 15 1934

It is Essential, Except Where Otherwise Provided in the Instructions, That This Form be Completely Filled In Irrespective of Any Statements, Schedules, or Reports Submitted Herewith

Cash | Check | M.O. | Date of Instl. Prem Payment

Date of Incorporation Dec. 14, 1928

Under the Laws of What State or Country Nevada

$

The Corporation's Books are in Care of _____ Located at _____

Kind of Business Trading Is This a Consolidated Return? No If so, of How Many Corporations? _____

If a Foreign Corporation, State Whether Resident or Nonresident _____ If Nonresident, State Amount of Income Included (Instructions on Page Gross Income, 4.

ATTACH REMITTANCE HERE

Item No. | Schedule

GROSS INCOME

1. Gross Sales (where inventories are an income-determining factor), $ _____ ; Less Returns and Allowances, $ _____ ; Net Sales				$ 98 662 09	
2. Less Cost of Goods Sold:					
(a) Inventory at beginning of year	$				
(b) Material or merchandise bought for manufacture or sale		90 337 42			
(c) Miscellaneous costs (From Schedule A, Column 1) (1) Salaries and wages, $ _____ ; (2) Other costs, $ _____ ; Total					
(d) Total of Items (a), (b), and (c)	$				
(e) Less inventory at end of year		6 500		83 837 49	
3. Gross Profit from Sales (Item 1 minus Item 2)				$ 8 424 60	
4. Gross Receipts (where inventories are not an income-determining factor)	$				
5. Less cost of operations (From Schedule A, Column 2) (a) Salaries and wages, $ _____ ; (b) Other costs, $ _____ ; Total					
6. Gross Profit where inventories are not an income-determining factor (Item 4 minus Item 5)					
7. Interest on Loans, Notes, Mortgages, Bonds, Bank Deposits, etc.				9 035 81	
8. Rents				495	
9. Royalties					
10. (a) Profit from Sale of Stocks and Bonds held 2 years or less. (From Schedule B, Total (c))				40 082 87	
(b) Profit or Loss from Sale of all other Assets. (From Schedule B, Total (b))					
11. Dividends on Stock of: (a) Domestic Corporations subject to taxation under Title I of Revenue Act of 1932				32	
(b) Domestic Corporations not subject to taxation under Title I of Revenue Act of 1932				17 541	
(c) Foreign Corporations					
13. Other Income (State nature of income) (Use separate schedule, if necessary)				22,078.01	
13. TOTAL INCOME (IN ITEMS 3, AND 6 TO 12, INCLUSIVE)				$ 76-410 3.90	$ 75 579 28

DEDUCTIONS

14. Compensation of Officers (From Schedule C)			$ None	
15. Rent on Business Property			1 140	
16. Repairs (From Schedule D): (a) Salaries and Wages, $ _____ (b) Other Costs, $ RAR Total 2149 33				
17. Interest				
18. Taxes (From Schedule E)			1 28418	
19. Losses by Fire, Storm, etc. (From Schedule F) Steamship Operations			4 41226	
20. Bad Debts (From Schedule G)			21 38404	
21. Dividends (From Schedule H)			17 541	
22. Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)			20 64985	
23. Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction H)				
24. Other Deductions Authorized by Law (Explain below, or on separate sheet)				
(a) Salaries and wages. (Not included in Items 2, 5, 14, or 15 above)			5 785	
(b) General Expense			3 50170	
25. TOTAL DEDUCTIONS (IN ITEMS 14 TO 24)				$ 75 698 03
26. NET INCOME (Item 13 minus Item 25)			Loss	$ 118 75

COMPUTATION OF TAX

Income Tax		Excess-Profits Tax	
27. Net Income (Item 26 above)	$	29. Net Income for Excess-profits Tax Computation (Item 26, above)	$
28. Less Income Tax Paid or Accrued (Not credit nor if deducted only by a Corporation Exempt by a Domestic Corporation)		30. Less 10% of $ _____ value of capital stock as declared for year ended Jan. 31, 1933 (or estimated value of capital stock if not previously declared for that period) (See Sec. 207, by those corporations of the calendar group not on capital-stock tax. If this is a consolidated return)	
29. Balance (Item 27 minus Item 28)		31. Amount Subject to Excess-profits Tax (Item 29 minus Item 30)	
		32. Excess-profits Tax (8% of Item 31)	

An amended return must be marked "Amended" at top of return. Checks and drafts will be accepted only if payable at par.

7-1

SCHEDULE B—BALANCE SHEETS (See Instruction 6)

Items	Beginning of Taxable Year — Amount	Beginning of Taxable Year — Total	End of Taxable Year — Amount	End of Taxable Year — Total
ASSETS				
1. Cash		$ 1 106 777 07		$ 1 022 125 45
2. Notes receivable		14 000		
3. Accounts receivable	$ 211 628 96		$ 312 062 56	
Less reserve for bad debts		211 328 96	2 160 50	309 901 86
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods			6 500	
Supplies				
				6 500
5. Investments (securities): Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended, and obligations of United States possessions				
Obligations of the United States				
6. Other investments:				
Stocks of domestic corporations	$ 1 000 945 50		$ 1 032 190 55	
Bonds of domestic corporations	15 425		15 445	
Stocks and bonds of foreign corporations				
All other investments or loans	122 500	1 136 866 50	106 000	1 150 635 55
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
All other				
8. Capital assets:				
Land	$ 20 000		$ 20 000	
Buildings	20 000		20 000	
Machinery and equipment	7 750 50		7 750 50	
Furniture and fixtures	5 000		5 000	
Delivery equipment				
	$ 62 750 50		$ 62 750 50	
Less reserves for depreciation (except on land)	9 250 50	53 500 00	12 400 35	50 350 15
9. Patents				
10. Good will				
11. Other assets (describe fully):	$		$	
12. Total Assets		$ 2 328 274 45		$ 2 539 510 71
LIABILITIES				
13. Notes payable (less than one year)		$		$
14. Accounts payable		2 064 68		2 378 71
15. Bonds and notes (not secured by mortgage)				
16. Mortgages (including bonds and notes so secured)				
17. Accrued expenses:				
Interest	$		$	
Taxes			40000	
All other				400 00
18. Other liabilities (describe fully):	$		$	
19. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)		2 500 000 00		2 500 000 00
20. Surplus	$		$	
21. Undivided profits		19 309 75		36 732 00
22. Total Liabilities		$ 2 522 374 43		$ 2 539 510 71

Remarks

SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from line 23, page 1 of this return	None			11	675		
2. Deductions not:							
(a) Interest on obligations of State, Territorial, or any political subdivision thereof, or the District of Columbia							
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended							
(c) Interest on obligations of the United States or its possessions							
(d) Dividends deductible under Section 26 (p) of the Revenue Act of 1926				17	841		
(e) Proceeds of life insurance policies paid upon the death of the insured							
(f) Other items of nontaxable income (to be itemized):							
(a)							
(b)							
(c)							
3. Charges against reserve for bad debts, if Item 13, page 1 of return, is not in addition to a reserve							
4. Charges against reserve for contingencies, etc. (to be itemized):							
(a)							
(b)							
(c)							
5. Total of Items 1 to 4, inclusive							
6. Total from Line 25							
7. Net profit for year, as shown by books, before any adjustments on such Schedule (Line 6 minus Line 5)							
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year				19	30975		
9. Other credits to surplus (to be itemized):							
(a)							
(b)							
(c)							
10. Total of Items 7 to 9, inclusive							
11. Total from Line 22							
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)				36	732	00	

13. Unallowable deductions:							
(a) Expenses, premiums, and contributions							
(b) Income and profits taxes paid to the United States, and such taxes paid to the possessions or foreign countries if claimed as a credit in Item 10, page 1 of the return							
(c) Federal taxes paid on tax-free covenant bonds							
(d) Special improvement taxes tending to increase the value of the property assessed							
(e) Penalties and fines, additions, or interest imposed or expenses on the basis							
(f) Disbursements not reported							
(g) Insurance premiums paid on the life of any officer or any person where the corporation is directly or indirectly a beneficiary							
(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation							
(i) Additions to reserve for bad debts which are not included in Item 13, page 1 of return							
(j) Additions to reserves for contingencies, etc. (to be itemized):							
(a)							
(b)							
(c)							
(k) Other nondeductible deductions (to be itemized):							
(a)							
(b)							
(c)							
14. Total of Line 13							
15. Dividends paid during the taxable year (more than 60 days after close of taxable year must be reported as a dividend in the following year) (see Par. (a) Section 115):							
(a) Date paid _____ Character _____						None	
(b) Date paid _____ Character _____							
(c) Date paid _____ Character _____							
(d) Date paid _____ Character _____							
16. Other debits to surplus (to be itemized):							
(a)							
(b)							
(c)							
17. Total of Lines 14 and 15							

NET INCOME OR DEFICIT REPORTED IN RETURN FOR 1928 BEFORE DEDUCTING NET LOSS FOR PRIOR YEAR

1. Enter amount of net income ~~or deficit~~ for 1928 before deducting net loss for 1921 $ 11,740.89

2. Enter amount deducted in return for 1928 on net loss for 1921 $ _____

KIND OF BUSINESS

3. State the main business engaged in, also whether acting as principal or as agent on commission; state if inactive or in liquidation:

_____

_____

Check the proper blank below to indicate the general industrial division in which the corporation's main income-producing business falls:

- ☐ Agriculture and related industries, including fishing, forestry, ice harvesting, etc.; also leasing of such property.
- ☐ Mining and quarrying, including gas and oil wells; also leasing of such property.
- Manufacturing—
  - ☐ Food products and beverages.
  - ☐ Tobacco.
  - ☐ Textiles and textile products.
  - ☐ Leather and leather products.
  - ☐ Rubber and related products.
  - ☐ Lumber and wood products, including finer furniture.
  - ☐ Paper, pulp and products.
  - ☐ Printing, publishing, and allied businesses.
  - ☐ Chemicals and allied products, including petroleum products.
  - ☐ Stone, clay, and glass products.
  - ☐ Metal and metal products, including precious metals and products.
  - ☐ Other manufacturing.
- ☐ Construction—construction, buildings, bridges, railroads, ships, etc.; also equipping and installing operating systems, elevators, or machinery within their manufacture.
- ☐ Transportation—rail, water, canal, motor, etc.; also leasing of such facilities.
- ☐ Public utilities—electric light or power, gas (artificial or natural), give steam, telephone, telegraph or radio, underwater, heating, toll bridges, etc.; also leasing of such utilities.
- ☐ Storage—cold storage, grain elevators, warehouses, safe deposit vaults, etc.; also leasing of such property.
- ☐ Trading—wholesale, retail, or commission.
- ☐ Service—professional, business, amusement, and domestic, including hotels, restaurants, laundries, etc.
- ☐ Finance—banks and other financial organizations, insurance, real estate; also brokers and agents.

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTIONS 40

4. Is this a consolidated return? No If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filed in, sworn to, and filed as a part of this return. See Section 141 of the Revenue Act of 1928 and Instruction 41.

5. Was the income of this corporation included in a consolidated return for the prior year? _____

If so, give name of corporation which filed the consolidated return. _____

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? Yes Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? _____ If answer is "yes," give name and address of such predecessor business, and the date of the change in entity. _____

_____

_____

Upon such change were any asset values increased or decreased? _____ If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of cash receipts and disbursements? Yes If not, describe fully what other basis or method was used in computing net income. _____

_____

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock. _____

COST

_____

_____

_____

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

_____

_____

_____

_____

_____

73

Schedule A

1. Cost of sales (where inventories are an income-determining factor)

[Not filled in]

2. Cost of operations (where inventories are not an income-determining factor)

[Not filled in]

Schedule B

Profit from Sale of Stocks, Bonds, Real Estate, etc.

[Not filled in]

Schedule C—Compensation of Officers

None

Schedule D—Cost of Repairs

[Not filled in]

Schedule E—Taxes Paid

[Not filled in]

Schedule F—Explanation of Losses by Fire, Storm, etc.

[Not filled in]

Schedule G—Bad Debts

[Not filled in]

Schedule H—Dividends Deductible

[Not filled in]

Schedule I—Explanation of Deduction for Depreciation

1. Kind of Property	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquisition	5. Cost	6. March 1, 1913, Value if Acquired Prior to That Date	7. Depreciation Allowed (or Allowable) in Prior Years	8. Depreciation Allowable This Year
Wooden Bldg.	Jan. 2, 1929		20 Years	$ 20,000	$	$1000.	$ 1000.
" Steamers	"	10 Years	10 "	175,000		8750.	17500.
Furniture & Fixtures	"		10 "	5,000		500.	500.
Autos		New	5 "	8,249.25		900.	1649.85

AFFIDAVIT

We, the undersigned, president (or vice president, or other principal officer) and treasurer (or assistant treasurer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1932 and the National Industrial Recovery Act and the Regulations issued thereunder.

F. A. WILSON

President

W. T. WILSON

[Corporate Seal] Secretary

Sworn to and subscribed before me this 15th day of March, 1934.

W. SHINE,

[Notarial Seal] Dep. Coll. [132]

NOTICE TO CORPORATIONS

This form should be executed and [illegible] Income Tax Form 1120 for the calendar year 1933. If the corporation merely [illegible] person or persons employed to assist in the preparation of the return, the name [illegible] advisor, together with a statement showing the extent to which such advice was received, is sufficient. If the return was

actually prepared by any such person or persons, this form must be signed and sworn to by such person or persons.

Did the corporation employ anyone especially to prepare or advise in the preparation of its income tax return for the calendar year 1933? (Answer "yes" or "no")—No. If so, give name and address and state to what extent such assistance or advice was received:

I/We, acting as.....(Attorney or advisor) for the hereto subscribed taxpayer, affirm that I/we prepared the return, that the information set out in the return and accompanying schedules, if any, correctly and truly represents the information furnished or discovered by me/us during the course of preparation of the return, and that such information is true to the best of my/our information and belief.

.....

(Attorney or advisor)

.....

(Address)

Sworn to and subscribed before me this.....day of....., 1934.

....

(Signature of officer administering oath) (Title)

[Notarial Seal] [133]

Form 1100
Treasury Department
Internal Revenue Service

RETURN OF INFORMATION

By Brokers and Other Agents—Calendar Year 1933

Name and address of guarantor of account:

Names and addresses of others with power to make withdrawals of cash, securities, or commodities from the account:

Name and address of customer and title of account:

Wilson Bros. & Co.,
1312 Russ Bldg.,
San Francisco, Calif.

Total purchases, $107,860. Total sales, $120,821.

Name and address of broker or agent:

Francis A. Wilson,
1312 Russ Bldg.,
San Francisco, Calif.

Instructions

Prepare this form in accordance with the instructions on return Form 1100-A. Forward with return Form 1100-A to reach the Commissioner of Internal Revenue, Sorting Section, Washington, D. C., on or before February 15, 1934. [134]

1933 RETURN OF CAPITAL STOCK TAX

For Year Ending June 30, 1933
Domestic Corporations
(Sec. 215, National Industrial Recovery Act,
73d Congress, Public, No. 67)

This return must be filed with the Collector of Internal Revenue for your district on or before July 31, 1933, and the tax must be paid on or before that date.

Duplicate 781
First California
Assessment List, Form 23A
Sep. 1933
43526

Examined by:

.....

1. Name—Wilson Bros. & Co.,
2. Address—1312 Russ Bldg., San Francisco, California
3. Name of parent company, if any— (District filed—)
4. Name of subsidiary, if any— No. shares held— (District filed—)
5. Nature of business in detail—Lumber & Shipping
6. Incorporated or organized in State of—Nevada
   Month—November Year—1928
   See Instructions on Reverse Side
7. Date of close of the last income-tax taxable year ending on or prior to the year ended June 30, 1933*—December 31, 1932.
   ***If no income-tax taxable year ending on or prior to year ended June 30, 1933, use date of organization.**
8. Capital account as shown on balance sheet as of the date set forth in item 7 (no other date should be used):

	Number of shares	Par value per share	Total
(a) Common stock	20		$2500000.
(b) First preferred stock			
(c) Second preferred stock—			
(d) Surplus (or deficit)			19300.75
(e) Undivided profits			
(f) Total			25019309.75

Computation of Tax

9.	Original declared value for entire capital stock as of the date shown in item 7	$400000.
10.	Tax at rate of $1 for each full $1,000 in item 9 (omit cents)	400.
11.	Penalty of 25 percent for delinquency in filing return	
12.	Interest	
13.	Total tax, penalty and interest	

Sep. 5, 1933

State of California,
County of San Francisco—ss:

We, F. A. Wilson, President, and W. T. Wilson, Treasurer, of the corporation for which this return for capital stock tax imposed by section 215 of the National Industrial Recovery Act is made, being severally duly sworn, each for himself, deposes and says that the items entered in the foregoing report, including any statements attached to or accompanying this return, are, to his best knowledge and belief and from such information as he has been able to obtain, true and correct.

F. A. WILSON
President.
W. T. WILSON
Treasurer.

Sworn to and subscribed before me this 31st day of August, 1933.
[Illegible]
[Illegible]
[Seal]
(Official capacity)

[Endorsed]: Petitioner's Exhibit No. 4. Admitted in evidence June 6, 1939. [135]

EXHIBIT 5

PETITIONER'S EXHIBIT No. 5

Form 1120
TREASURY DEPARTMENT
Internal Revenue Service

FILED WITH THIS RETURN

CORPORATION INCOME AND EXCESS-PROFITS TAX RETURN
For Calendar Year 1934

or Fiscal Year beginning _____, 1934, and ended _____, 1935

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

WILSON BROS. & CO.
1112 - Russ Building.
(Number and street)
San Francisco, California.
(Post office and State)

It is Essential, Except Where Otherwise Provided in the Instructions, That This Form be Completely Filled In Irrespective of Any Statements, Schedules, or Reports Submitted Herewith

Date of Incorporation Dec. 14, 1928

Under the Laws of what State or Country Nevada

Page 1 of Return

No. Cash 1571

Serial Number 855786

Region 1 Calif.
(Collector's District)

Cash | Check | M.O. | Cert. of Ind. | Date Payment

$

13,632.27
Sup- 681.64

RAC

The Corporation's Books are in Care of _____ Located at _____

Kind of Business (in detail) Wholesale Lumber (Also check industrial division on page 3) Is This a Consolidated Return of Affiliated Corporations? No If so, of How Many Corporations? _____

If a Foreign Corporation, State Whether Resident or Nonresident _____; If Nonresident, State Amount of Income Excluded (Instruction on Form Gross Income, $ _____

Is the Corporation a personal holding company within the meaning of Section 351 of the Revenue Act of 1934? No (Answer "yes" or "no") (If so, an additional return on Form 1120 H must be filed.)

ATTACH REMITTANCE HERE

GROSS INCOME

1. Gross Sales (where inventories are not an income-determining factor), $ _____ ; Less Returns and Allowances, $ _____ ; Net Sales			$ 170 239 51	
2. Less Cost of Goods Sold:				
(a) Inventory at beginning of year	$ 6 500			
(b) Material or merchandise bought for manufacture or sale	147 533 55			
(c) Miscellaneous costs (From Schedule A, Column D: (1) Salaries and wages, $ _____ ; (2) Other costs, $ _____ ; Total				
(d) Total of Items (a), (b), and (c)	154 033 55			
(e) Less inventory at end of year	3 946 60		150 086 95	
3. Gross Profit from Sales (Item 1 minus Item 2)			$ 20 152 56	
4. Gross Receipts (where inventories are not an income-determining factor) $				
5. Less cost of operations (From Schedule A, Column D: (a) Salaries and wages, $ _____ ; (b) Other costs, $ _____ ; Total				
6. Gross Profit where inventories are not an income-determining factor (Item 4 minus Item 5)				
7. Interest on Loans, Notes, Mortgages, Bonds, Bank Deposits, etc.			14 400 44	
8. Rents			597	
9. Royalties				
10. Capital Gain or Loss (From Schedule D)			3 694 60	
11. Interest on Liberty Bonds, etc. (From Schedule J)				
12. Dividends on Stock of: (a) Domestic Corporations subject to taxation under Title I of Revenue Act of 1934				
(b) Domestic Corporations not subject to taxation under Title I of Revenue Act of 1934			25 057	
(c) Foreign Corporations				
13. Other Income (State nature of business) (Use separate schedule, if necessary)				
14. TOTAL INCOME OF ITEMS 3, AND 6 TO 13, INCLUSIVE				$ 63 901 40

DEDUCTIONS

15. Compensation of Officers (From Schedule C)		None	
16. Rent on Business Property		1 140	
17. Repairs (From Schedule D): (a) Salaries and Wages, $ _____ ; (b) Other Costs, $ _____ ; Total			
18. Interest			
19. Taxes (From Schedule E)		396 09	
20. Losses by Fire, Storm, etc. (From Schedule F) Steamship operations		2 173 18	
21. Bad Debts (From Schedule G)		15 144 40	
22. Dividends (Item 12 as above)		25 057	
23. Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)		11 399 85	
24. Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see instruction 8)			
25. Other Deductions Authorized by Law (Explain below, or on separate sheet)			
(a) Salaries and wages. (Not included in Items 5, 6, 15, or 17 above)		5 815	
(b) General Expense		4 119 84	
26. TOTAL DEDUCTIONS OF ITEMS 15 TO 25			$ 65 242 96
27. NET INCOME (Item 14 minus Item 26)		Loss	$ 1 341 56

COMPUTATION OF TAX

Income Tax

28. Net Income (Item 27, above) $
29. Less Interest on Liberty Bonds, etc. (Item 11)
30. Balance subject to Income Tax (Item 28 minus Item 29)
31. Income Tax (13½% of Item 30) (or 12½% of Item 30, if this is a consolidated return of affiliated corporations)
32. Less Income Tax Paid at Source (Title I, Revenue Act of 1934) (Attach one (1) statement only to a consolidated foreign corporation return)
33. Income Tax Paid to a Foreign Country or U. S. Possession by a Domestic Corporation
34. Balance of Income Tax (Item 31 minus Items 32 and 33)

Excess-Profits Tax

35. Net Income for Excess-profits Tax Computation (Item 27, above)
36. Less: 8% of U. S. value of capital stock as determined by your capital-stock tax return for year ended June 30, 1934
37. Amount Subject to Excess-profits Tax (Item 35 minus Item 36)
38. Excess-profits Tax (6% of Item 37)

Note.—Separate computation of Excess-profits Tax must be made on Form 1120 by each member of an affiliated group of railroad corporations making a consolidated Income Tax return.

50-1

SCHEDULE L—BALANCE SHEETS (See Instruction 14)

Item	Beginning of Taxable Year		End of Taxable Year	
	Amount	Total	Amount	Total
ASSETS				
1. Cash		$ 1 022 125 45		$ 972 147 49
2. Notes receivable			$ 347 661 49	
3. Accounts receivable	$ 51 062 34			
(a) Less reserve for bad debts	1 160 00	207 901 56	6 884 90	340 776 59
4. Inventories:				
(a) Raw materials	$		$	
(b) Work in process				
(c) Finished goods	6 500		3 946 60	
(d) Supplies				
		6 500 00		3 946 60
5. Investments (nontaxable):				
(a) Obligations of a State, Territory, or any political subdivision thereof, or District of Columbia, or United States possessions	$		$	
(b) Obligations of instrumentalities of the United States				
(c) Obligations of the United States				
6. Other investments:				
(a) Stocks of domestic corporations	$ 1 032 190 55		$ 1 077 778 05	
(b) Bonds of domestic corporations	13 445		24 745	
(c) Stocks and bonds of foreign corporations				
(d) All other investments or loans	106 000	1 150 635 55	96 600	1199 123 05
7. Deferred charges:				
(a) Prepaid insurance	$		$	
(b) Prepaid taxes				
(c) All other				
8. Capital assets:				
(a) Land	$ 20 000		$ 20 000	
(b) Buildings	20 000		20 000	
(c) Machinery and equipment	7 750 80		7 750 80	
(d) Furniture and fixtures	5 000		5 000	
(e) Delivery equipment				
	$ 62 750 80		$ 62 750 80	
(f) Less reserves for depreciation (except on land)	12 400 56	50 350 24	15 050 20	47700 60
9. Patents				
10. Good will				
11. Other assets (describe fully):				
	$		$	
12. TOTAL ASSETS		$ 2 539 510 71		$ 2565 696 93
LIABILITIES				
13. Notes payable (less than one year)		$		$
14. Accounts payable		2 978 71		3 246 39
15. Bonds and notes (not secured by mortgage)				
16. Mortgages (including bonds and notes so secured)				
17. Accrued expenses:				
(a) Interest	$		$	
(b) Taxes	400			
(c) All other		400		
18. Other liabilities (describe fully):				
	$		$	
19. Capital stock:				
(a) Preferred stock (less stock in treasury)	$		$	
(b) Common stock (less stock in treasury)		2 500 000 00		2 536 000 00
20. Surplus	$		$	
21. Undivided profits		34 732 00		23 447 64
22. TOTAL LIABILITIES		$ 2 539 510 71		$ 2565 696 93

Remarks

D-2

SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 30, page 1 of the return
2. Nontaxable income:
   (a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia, or United States possessions
   (b) Interest on obligations of the United States (except interest in excess of exemption as reported in Schedule J (c))
   (c) Dividends deductible under Section 26 (p) of the Revenue Act of 1934
   (d) Proceeds of life insurance policies paid upon the death of the insured
   (e) Other items of nontaxable income (to be detailed):
   (1)
   (2)
   (3)
3. Charges against reserve for bad debts, if Item 21, page 1 of return, is not an addition to a reserve
4. Charges against reserves for contingencies, etc. (to be detailed):
   (a)
   (b)
   (c)
5. Total of Lines 1 to 4, inclusive
6. Total from Line 14
7. Net profit or loss for year, as shown by books, before any adjustments are made thereon (Line 5 minus Line 6) (If loss, indicate)
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year
9. Other credits to surplus (to be detailed):
   (a)
   (b)
   (c)
10. Total of Lines 7 to 9, inclusive
11. Total from Line 17
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)

13. Unallowable deductions:
   (a) Donations, gratuities, and contributions
   (b) Income and profits taxes paid to the United States, and such taxes paid to the possession or foreign ownership if claimed as a credit to them or in part to Item 32, page 1 of the return
   (c) Federal taxes paid on tax-free government bonds
   (d) Special improvement taxes tending to increase the value of the property assessed
   (e) Purchases and futures, additions, or betterments treated to expense on the books
   (f) Replacements and renewals
   (g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary
   (h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation
   (i) Additions to reserves for bad debts in excess of amount included in Item 21, page 1 of return
   (j) Additions to reserves for contingencies, etc. (to be detailed)
   (1)
   (2)
   (3)
   (k) Other unallowable deductions (to be detailed)
   (1)
   (2)
   (3)
14. Total of Line 13
15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):
   (a) Date paid ..... Character .....
   (b) Date paid ..... Character .....
   (c) Date paid ..... Character .....
   (d) Date paid ..... Character .....
16. Other debits to surplus (to be detailed)
   (a)
   (b)
   (c)
17. Total of Lines 15 and 16

NET INCOME (OR DEFICIT) REPORTED IN RETURN FOR CALENDAR YEAR 1935 OR FISCAL YEAR 1935

1. Net income, $ ..... for deficit ..... $ .....

NATURE OF BUSINESS

2. Check the blank to indicate the industrial division in which the corporation's main business was conducted:

- ☐ Agriculture and related industries, including fishing, forestry, ice-harvesting, hunting and trapping
- ☐ Mining and quarrying, including gas and oil wells, mining rock properties
- ☐ Building and construction

MANUFACTURING

Food and kindred products:
- ☐ Bakery and confectionery products
- ☐ Canned products—fish, fruit, vegetables, preserves
- ☐ Mill products—feed, flour, meal
- ☐ Packing-house products—meats, lard, sausage casings
- ☐ Sugar—cane, cane, maple, molasses, sirups, refineries
- ☐ Other food products—butter substitutes, cereals, cocoa, spices, dairy products, artificial ice, etc.
- ☐ Beverages, soft drinks, mineral waters
- ☐ Brewing and distilling—alcohol, liquors, beer, malt extract, vinegar
- ☐ Tobacco products

Textiles:
- ☐ Cotton goods—dress goods, etc.; supplies, dyeing
- ☐ Woolen and worsted goods—dress goods, etc.; wool pulling, scouring, etc.
- ☐ Silk and rayon goods—dress goods, thrown silk, etc.; spinning, weaving
- ☐ Carpets, floor coverings, tapestries, linoleum
- ☐ Other textiles—cord, felt, fur, linen, artificial leather, sanitary textiles, etc.
- ☐ Clothing—men's, women's, children's—made, underwear, millinery, etc.
- ☐ Knit goods—underwear, hosiery, etc.
- ☐ Leather boots, shoes, slippers, etc.
- ☐ Other leather products—saddlery, harness, trunks, handbags, tanning
- ☐ Rubber tires and tubes
- ☐ Other rubber goods—boots, shoes, heels, soles, mechanical rubber
- ☐ Bone, celluloid and ivory products
- ☐ Paperstill and planing mill products
- ☐ Other wood products—cooperage, wagons, furniture, toys, etc.
- ☐ Paper, pulp and products
- ☐ Printing, publishing, and allied industries
- ☐ Petroleum and other mineral oil refining and products
- ☐ Chemicals, paints, acids, compounds, and not products, etc.
- ☐ Allied chemical substances, drugs, oils, soaps, etc.
- ☐ Paints, pigments, varnishes, etc.
- ☐ Fertilizers
- ☐ Stone, clay, glass, and mineral products

MANUFACTURING—(Continued)

Metal products and processes:
- ☐ Iron and steel—products of blast furnaces, rolling mills, foundries
- ☐ Locomotives and railroad equipment
- ☐ Motor vehicles, complete or parts
- ☐ Machinery—factory, used in producing food, lumber, textiles, paper, leather, metals, stone, clay, glass, metals and wood products
- ☐ Machinery—agricultural and equipment
- ☐ Machinery—electrical and equipment
- ☐ Machinery—other, building, construction, gas and mining machinery and equipment
- ☐ Household equipment—metal furniture, safes, stoves, sewing machines, washing machines, etc.
- ☐ Office equipment
- ☐ Metal building material and equipment
- ☐ Hardware, tools, etc.
- ☐ Precious metal products and processes
- ☐ Other metals, products and processes

Miscellaneous manufacturing:
- ☐ Rubber, complete or parts
- ☐ Musical, professional, and scientific instruments, optical goods, small boats
- ☐ Airplanes, complete, equipment, parts
- ☐ Communication—construction, bridges, buildings, railroads, shops, conveying and handling systems
- ☐ Transportation—rail, water, aerial, motor, or , including such facilities
- ☐ Public utilities—electric light or power, gas (natural or manufactured), pipe lines, telegraph, telephone, water-works, local transit, local bridges, etc., including such utilities
- ☐ Trade, retail, storage, grain elevators, warehouses, cold storage, yards, etc.

Trade:
- ☐ Wholesale
- ☐ Retail
- ☐ Wholesale and retail
- ☐ Commission

- ☐ All other trade—repair service, garages for storage, live animals, etc.
- ☐ Service—hotels, restaurants, amusement, domestic, and all other

Finance:
- ☐ Banks—national, State, private, savings, joint-stock land banks
- ☐ Stock and bond brokers, investment bankers or brokers, investment trusts
- ☐ Real estate, realty holding, and estate agents
- ☐ Insurance companies (not agents)
- ☐ Other finance—loan companies, building and loan associations, trusts, mortgage or pawn brokers, stock exchanges, insurance agents,

AFFILIATIONS WITH OTHER CORPORATIONS (See Instruction 39)

3. Is this a consolidated return? ..... If so, pursuant from the collector of in revenue for your district Form 851, Affiliations Schedule, which shall be filed in, sworn to, and file part of this return.

4. Was the income of this corporation included in a consolidated return for the prior year? .....

If so, give name of corporation which filed the consolidated return.

PREDECESSOR BUSINESS

5. Did the corporation file a return under the same name for the preceding taxable year? Yes

Was the corporation in any way an outgrowth, result, continuation, or reorganization of a taxable

businesses or extension during this or any prior year since December 31, 19?

answer is "yes", give name and address of such predecessor business, and the date of the change to or

Upon such change were any asset values increased or decreased?

If the answer is "yes", showing balance sheets of old business and opening balance sheets of new be must be furnished.

BASIS OF RETURN

6. Is this return made on the basis of cash receipts and disbursements? Yes

If not, describe fully what other basis or method was used in computing net income.

VALUATION OF INVENTORIES

7. State whether the inventories at the beginning and end of the taxable year were valued at c cost or market, whichever is lower. If other basis was used, describe fully, state why used and th inventory was last reconciled with cost. Cost

PREPARATION OF RETURN (See Instruction 32)

8. Did any person or persons advise the corporation in respect of any question or matter affecting items or schedules of this return, or assist or advise the corporation in the preparation of this ret actually prepare this return for the corporation? No If so, give the name and add such person or persons and state the nature and extent of the assistance or advice rendered and the and schedules in respect of which the assistance or advice was rendered, if this return was actually paved by any person or persons other than the corporation, state the reasons of the information upon

this return and the manner in which it was furnished to or obtained by such person or persons.

INFORMATION RETURN

9. Did the corporation make a return of information on Forms 1096 and 1099 (see Instruction 37) f

calendar year 1934? (Answer "yes" or "no")

LIST OF ATTACHED SCHEDULES

10. Enter below a list of all schedules accompanying this return, giving for each a brief title or schedule number. The name and address of the corporation should be placed on each separate sch

accompanying the return.

Page 4 of Return

SCHEDULE A (See Instructions 3 and 8)

1. COST OF SALES (WHERE INVENTORIES ARE AN INCOME-DETERMINING FACTOR)		2. COST OF OPERATIONS (WHERE INVENTORIES ARE NOT AN INCOME-DETERMINING FACTOR)	
Items	Amount (Same as Item 3 (c))	Items	Amount (Same as Item 9)
Salaries and wages	$	Salaries and wages	$
Other costs		Other costs	

SCHEDULE B—CAPITAL GAINS AND LOSSES (See Instruction 10)

1. Description of Property	2. Date Acquired	3. Date Sold	4. Amount Received	5. Cost	6. March 1, 1913, Value if Acquired Before That Date	7. Cost or Interpolated Value After Acquisition on March 1, 1913	8. Depreciation Allowed (or Allowable) Since Acquisition on March 1, 1913 (Percent details)	9. Gain or Loss
	Mo. Day Year	Mo. Day Year	$	$	$	$	$	$

Net Gain or Loss (enter as Item 10) (Capital losses are allowable only to the extent of $2,000 plus capital gains) $

State (1) how property was acquired ; (2) whether at time of sale or exchange purchaser owned more than 50% in value of your outstanding stock

Every sale or exchange of stock should be reported in detail, including name and address of corporation, class of stock, number of shares, capital changes affecting basis (stock dividends, other nontaxable dividends, stock rights, etc.)

Cost of property must be entered in column 5 if a loss is claimed in column 9

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 13)

1. Name and Address of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned		5. Amount of Compensation (Enter on Item 14)
			4. Common	5. Preferred	
					$ NONE

NOTE: Schedule C-1 also must be filed with this return if compensation in excess of $15,000 was paid to any officer or employee.

SCHEDULE D—COST OF REPAIRS (See Instruction 17)

1. Items	2. Amount (Enter on Item 17)
Salaries and wages	$
Other costs	

SCHEDULE E—TAXES PAID (See Instruction 19)

1. Items	2. Amount (Enter on Item 19)
	$

SCHEDULE F—EXPLANATION OF DEDUCTION FOR LOSSES BY FIRE, STORM, ETC. (See Instruction 20)

1. Kind of Property	2. Date Acquired	3. Cost	4. Subsequent Improvements	5. Depreciation Allowable Since Acquisition	6. Insurance and Salvage Value	7. Deductible Loss (Enter on Item 20)
		$	$	$	$	$

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 21)

1. Year	2. Sales on Account	3. Bad Debts
1930	$	$
1931		
1932		
1933		
1934		

SCHEDULE H—INCOME FROM DIVIDENDS (See Instruction 12)

Enumerate below all dividends received during the year, stating the amounts and the name and address of the corporations which declared the dividend

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 22)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Cost or March 1, 1913 Value if Acquired Prior to That Date (Indicate basis)	4. Amount Fully Depreciated in Use to End of Year	5. Depreciation or Allowed on Prior Years	6. Remaining Cost or Other Base on Re-Estimated	7. Life Used in Arriving Depreciation	8. Estimated Remaining Life from Beginning of Year	9. Depreciation Allowable This Year
Wooden Bldg.	Jan 1923	20,000		5,000	15,000	5 yrs	15 yrs	500 00
" Steamers	"	175,000		70,000	105,000	"	5 "	8750 00
Furniture	"	4,000		2,000	2,000	10 "	5 "	200 00
Autos	"	4,000		2,850	1,150	4½ "	2 Mons.	1249 85

SCHEDULE J—INTEREST ON LIBERTY BONDS AND OTHER OBLIGATIONS OR SECURITIES (See Instruction 11)

1. Obligations or Securities	2. Amount Owned	3. Interest Received or Accrued	4. Principal Amount Exempt from Taxation	5. Amount Owned at Future or Exemption	6. Interest on Amount in Future or Exemption (Enter on Item 11)
(a) Obligations of a State, Territory or political subdivision thereof, or the District of Columbia, or United States possessions	$	$	All	$	$
(b) Obligations issued under Federal Farm Loan Act, or under such Act as amended			All		
(c) Liberty 3½% Bonds and other obligations of United States issued on or before September 1, 1917			All		
(d) Treasury Notes, Treasury Bills, and Treasury Certificates of Indebtedness			All		
(e) Liberty 4% and 4½% Bonds and Treasury Bonds			All		
(f) Obligations of instrumentalities of the United States (other than obligations to be reported in line (d) above)			None		

AFFIDAVIT (See Instruction 50)

We, the undersigned, president (or vice president, or other principal officer) and treasurer (or assistant treasurer, or chief accounting officer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return (including its accompanying schedules and statements, if any) has been examined by him and is, to the best of [illegible] knowledge and belief, a true, correct, and complete return, made for the fiscal [illegible] for the taxable year stated, pursuant to the Revenue Act of 1934 and the Regulations issued thereunder.

Sworn to and subscribed before me this [illegible] day of [illegible], 193[illegible]

NOTARIAL SEAL

(Signature of officer administering oath) (Title)

CORPORATE SEAL

(Signature of officer) (Title)

AFFIDAVIT (See Instruction 51)

I/we swear (or affirm) that I/we prepared this return for the person named herein and that the return (including its accompanying schedules and statements, if any) is a true, correct, and complete statement of all the information respecting the income tax and/or excess-profits tax liability of the person for whom this return has been prepared of which I/we have any knowledge.

Sworn to and subscribed before me this _____ day of _____, 193[illegible]

NOTARIAL SEAL

(Signature of person preparing the return)

(Signature of person preparing the return)

(Signature of officer administering oath) (Title) (Name of firm or employer, if any)

A-4

1934 RETURN OF CAPITAL-STOCK TAX

For year ending June 30, 1934
Domestic Corporations
(Sec. 701, Revenue Act of 1934, 73d Congress,
Public, No. 216)

This return must be filed with the Collector of Internal Revenue for your district on or before July 31, 1934, and the tax must be paid on or before that date.

Duplicate 1571
First-California
September, 1934
(Page) 4413 (Line) 4

Examined by: .....

1. Name Wilson Bros. & Co.
2. Address 1312 Russ Bldg., San Francisco, Calif.
3. Name of parent company, if any.....
   (District filed.....)
4. Name of subsidiary, if any.....
   No. shares held..... (District filed.....)
5. Nature of business in detail Wholesale Lumber.
6. Incorporated or organized in State of Nevada.
   Month December. Year 1928.

Declaration of the Value of the Capital Stock

Important.—Before declaring a value for the capital stock, carefully read the instructions below, as a value once declared cannot later be amended.

If you file your income tax return on a calendar year basis, or would do so if subject to income tax,

declare in the space below a value for the entire capital stock of your corporation as of December 31, 1933, which you are willing to have accepted in this and subsequent years, as a basis, subject to statutory adjustments, on which to pay capital-stock tax and excess-profits tax.

If you file your income-tax return on a fiscal year basis, or would do so if subject to income tax, declare the value as of the close of such fiscal year.

If your corporation was organized during the year July 1, 1933, to June 30, 1934, both dates inclusive, and if neither the first calendar year nor the first fiscal year for income-tax purposes has ended during the year July 1, 1933, to June 30, 1934, both dates inclusive, declare the value as of the date of organization.

If your corporation is without a capital stock represented by shares, declare a value for the net worth of the corporation.

(See Instruction No. 3 for additional information)

7. *Value of Entire Capital Stock $400,000.

Exemptions. (See Instruction No. 4)

8. Is exemption from the tax claimed? Answer Yes or No. (.....).
9. If exemption is claimed, check the block which shows basis of claim and furnish the information required on page 2.
   - ☐ Section 101, Revenue Act of 1934.
   - ☐ Insurance company.
   - ☐ Not doing business.

---

*A specific and unqualified value must be shown in this space. If the capital stock is of no value insert the word "None."

Computation of Tax	For use of Taxpayer	For use of Department
10. Amount shown in item 7	$400000	$
11. Tax at rate of $1 for each full $1,000 in item 10 (omit cents)	400	
12. Penalty of 25 percent for delinquency in filing return		
13. Interest		[Stamped] 8524
14. Total tax, penalty, and interest	400	

Affidavit

We, the undersigned, president (or vice president, or other principal officer) and treasurer (assistant treasurer or chief accounting officer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1934 and the Regulations issued thereunder.

[Corporate Seal] F. A. WILSON
President
W. T. WILSON
Treasurer.

Sworn to and subscribed before me this 30th day of Aug., 1934.

[Notarial Seal] C. MEHEGAN. [140]
D.C.

REVENUE ACT OF 1934

Title V—Capital-Stock and Excess-Profits Taxes

Section 701. Capital-Stock Tax

(a) For each year ending June 30, beginning with the year ending June 30, 1934, there is hereby imposed upon every domestic corporation with respect to carrying on or doing business for any part of such year an excise tax of $1 for each $1,000 of the adjusted declared value of its capital stock.

(b) For each year ending June 30, beginning with the year ending June 30, 1934, there is hereby imposed upon every foreign corporation with respect to carrying on or doing business in the United States for any part of such year an excise tax equivalent of $1 for each $1,000 of the adjusted declared value of capital employed in the transaction of its business in the United States.

(c) The taxes imposed by this section shall not apply:

(1) to any corporation enumerated in section 101;

(2) to any insurance company subject to the tax imposed by section 201, 204, or 207;

(3) to any domestic corporation in respect of the year ending June 30, 1934, if it did not carry on or do business during a part of the period from the date of the enactment of this act to June 30, 1934, both dates inclusive; or

(4) to any foreign corporation in respect of the year ending June 30, 1934, if it did

not carry on or do business in the United States during a part of the period from the date of the enactment of this act to June 30, 1934, both dates inclusive.

(d) Every corporation liable for tax under this section shall make a return under oath within one month after the close of the year with respect to which such tax is imposed to the collector for the district in which is located its principal place of business or, if it has no principal place of business in the United States, then to the collector at Baltimore, Md. Such return shall contain such information and be made in such manner as the Commissioner, with the approval of the Secretary, may by regulations prescribe. The tax shall, without assessment by the Commissioner or notice from the collector, be due and payable to the collector before the expiration of the period for filing the return. If the tax is not paid when due, there shall be added as part of the tax, interest at the rate of 1 per centum a month from the time when the tax became due, until paid. All provisions of law (including penalties) applicable in respect of the taxes imposed by section 600 of the Revenue Act of 1926 shall, insofar as not inconsistent with this section, be applicable in respect of the taxes imposed by this section. The Commissioner may extend the time for making the returns and paying the taxes imposed by this section, under such rules and regulations as he may prescribe, with the approval of the Secre-

tary, but no such extension shall be for more than 60 days.

(e) Returns required to be filed for the purpose of the tax imposed by this section shall be open to inspection in the same manner, to the same extent, and subject to the same provisions of law, including penalties, as returns made under title II of the Revenue Act of 1926.

(f) For the first year ending June 30 in respect of which a tax is imposed by this section upon any corporation, the adjusted declared value shall be the value, as declared by the corporation in its first return under this section (which declaration of value cannot be amended), as of the close of its last income-tax taxable year ending at or prior to the close of the year for which the tax is imposed by this section (or as of the date of organization in the case of a corporation having no income-tax taxable year ending at or prior to the close of the year for which the tax is imposed by this section). For any subsequent year ending June 30, the adjusted declared value in the case of a domestic corporation shall be the original declared value plus (1) the cash and fair market value of property paid in for stock or shares, (2) paid in surplus and contributions to capital, (3) its net income, (4) the excess of its income wholly exempt from the taxes imposed by title I over the amount disallowed as a deduction by section 24(a) (5) of such title, and (5) the amount of the dividend deduction allowable for income-tax purposes, and minus (A) the value of property dis-

tributed in liquidation to shareholders, (B) distribution of earnings or profits, and (C) the excess of the deductions allowable for income-tax purposes over its gross income; adjustment being made for each income-tax taxable year included in the period from the date as of which the original declared value was declared to the close of its last income-tax taxable year ending at or prior to the close of the year for which the tax is imposed by this section. The amount of such adjustment for each such year shall be computed (on the basis of a separate return) according to the income-tax law applicable to such year. For any subsequent year ending June 30, the adjusted declared value in the case of a foreign corporation shall be the original declared value adjusted (for the same income-tax taxable years as in the case of a domestic corporation), in accordance with regulations prescribed by the Commissioner, with the approval of the Secretary, to reflect increases or decreases in the capital employed in the transaction of its business in the United States.

Section 702. Excess-Profits Tax

(a) There is hereby imposed upon the net income of every corporation, for each income-tax taxable year ending after the close of the first year in respect of which it is taxable under section 701, an excess-profits tax equivalent to 5 per centum of such portion of its net income for such income-tax taxable year as is in excess of 12½ per centum of the adjusted declared value of its capital stock (or in the case of a foreign corporation the adjusted de-

clared value of capital employed in the transaction of its business in the United States) as of the close of the preceding income-tax taxable year (or as of the date of organization if it had no preceding income-tax taxable year) determined as provided in section 701. If the income-tax taxable year in respect of which the tax under this section is imposed is a period of less than 12 months, such adjusted declared value shall be reduced to an amount which bears the same ratio thereto as the number of months in the period bears to 12 months. For the purposes of this section the net income shall be the same as the net income for income-tax purposes for the year in respect of which the tax under this section is imposed.

(b) All provisions of law (including penalties) applicable in respect of the taxes imposed by title I of this act, shall, insofar as not inconsistent with this section, be applicable in respect of the tax imposed by this section, except that the provisions of section 131 of that title shall be not applicable.

Section 703. Capital-Stock Tax and Excess-Profits Tax Imposed by National Industrial Recovery Act

Sections 217(d) and (e) of the National Industrial Recovery Act are amended to read as follows:

"(d) The capital-stock tax imposed by section 215 shall not apply to any taxpayer in respect of any year except the year ending June 30, 1933.

"(e) The excess-profits tax imposed by section 216 shall not apply to any taxpayer in re-

spect of any taxable year ending after June 30, 1934."

[Endorsed]: Petitioner's Exhibit No. 5. Admitted in evidence June 6, 1939. [141]

PETITIONER'S EXHIBIT 6

Wilson Bros. and Co.

CASH IN BANKS

As at Dates Shown Hereunder

	January 1, 1932	December 31st, 1932	1933	1934
San Francisco Bank	$403,750.00	$51,324.00	none	none
Crocker First Nat'l Bank	—25.25	23,989.81	$ 539.04	$ 142.48
Wells Fargo Bank	320.83	21,324.42	8,647.39	21,415.06
Bank of America	259.79	none	none	52,149.82
Anglo California National Bank	4,694.28	none	none	none
	$408,999.65	$96,638.23	$9,186.43	$73,707.36

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PETITIONER'S EXHIBIT 7

Wilson Bros. and Co.

STOCKS OF DOMESTIC CORPORATIONS

As at January 1, 1932

Number of Shares	Security	Cost	Approximate Market Value
400	Anglo National Corporation	$ 21,000.00	$ 6,800.00
900	Canadian Pacific R. R. Co.	16,257.50	10,012.50
300	Continental Oil Co.	1,842.50	1,800.00
203	Electric Bond and Share Co.	4,937.50	2,207.62
100	Gulf Oil Co.	3,307.50	2,675.00
1,100	Great Northern R. R. Co.	23,362.50	19,250.00
100	International Harvester Co.	3,832.50	2,400.00
700	The National Cash Register Co.	9,752.50	5,687.50
300	Northern Pacific R. R. Co.	4,952.50	4,762.50
500	New York Central R. R. Co.	27,495.00	14,500.00
500	The Ohio Oil Co.	3,650.00	2,812.50
500	The Pennsylvania Railroad Co.	9,250.00	9,062.50
200	Royal Dutch Co.	2,722.50	2,825.00
500	Standard Oil Co. of Indiana	8,850.00	7,250.00
700	Standard Oil Co. of Kentucky	9,872.50	9,625.00
200	Socony Vacuum Oil Co.	1,977.50	1,825.00
900	Standard Oil Co. of California	24,905.00	22,500.00
900	Southern Pacific R. R. Co.	44,342.50	24,975.00
400	Simmons Company	3,655.00	3,000.00
2,100	Shell Union Oil Co.	9,242.50	6,300.00
2,238	Transamerica Corp.	139,595.00	5,595.00
800	The Texas Corporation	12,165.00	9,600.00
400	Underwood Elliott Fisher Co.	10,862.50	6,400.00
200	Union Oil Associates	3,197.50	2,225.00
1,100	Union Oil Co.	15,642.50	14,025.00
2,500	Weeden and Co.	100,000.00	75,000.00
		$516,670.00	$273,115.12

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PETITIONER'S EXHIBIT 8

Wilson Bros. and Co.

STOCKS OF DOMESTIC CORPORATIONS

As at December 31, 1932

Number of Shares	Security	Cost	Approximate Market Value
200	A. T. & S. F. Railway	$ 13,320.00	$ 8,075.00
1,652	Byron Jackson Co.	13,168.50	2,065.00
400	Anglo National Corporation	21,000.00	4,100.00
4,500	Continental Oil Co.	26,262.50	27,000.00
1,900	Canadian Pacific Railroad	27,932.50	27,312.50
303	Electric Bond and Share Co.	5,935.00	5,567.62
200	Gulf Oil Co.	6,277.50	5,300.00
3,500	Great Northern R. R. Co.	61,732.50	28,000.00
100	International Harvester Co.	3,832.50	2,175.00
2,400	National Cash Register Co.	24,572.50	18,300.00
900	Northern Pacific R. R.	12,807.50	12,037.50
1,400	New York Central R. R. Co.	49,965.00	26,425.00
1,300	The Ohio Oil Co.	10,610.00	8,775.00
800	The Pennsylvania Railroad Co.	13,877.50	11,400.00
1,000	Royal Dutch Co.	14,175.00	20,750.00
500	Standard Oil Co. of Indiana	8,850.00	10,875.00
1,400	Standard Oil Co. of Kentucky	18,495.00	14,875.00
200	Socony Vacuum Oil Co.	1,977.50	1,525.00
1,100	Standard Oil Co. of California	29,855.00	26,812.50
1,500	Southern Pacific R. R. Co.	58,502.50	24,187.50
400	Simmons Co.	3,655.00	2,600.00
3,600	Shell Union Oil Co.	14,642.50	18,900.00
2,238	Transamerica Corp.	139,595.00	12,029.25
1,800	The Texas Corp.	23,340.00	25,200.00
500	Underwood Elliott Fisher Co.	12,380.00	6,000.00
400	United Fruit Co.	7,470.00	9,500.00
200	Union Oil Associates	3,197.50	12,675.00
1,100	Union Oil Co. of California	23,515.00	
2,500	Weeden and Co.	100,000.00	62,500.00
		$750,943.50	$434,961.87

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PETITIONER'S EXHIBIT 9

Wilson Bros. and Co.

STOCKS OF DOMESTIC CORPORATIONS

As at December 31, 1933

Number of Shares	Security	Cost	Approximate Market Value
300	A. T. & S. F. Railway	$ 17,940.00	$ 16,875.00
1,652	Byron Jackson Co.	13,168.50	6,814.50
400	Anglo National Corp.	21,000.00	1,260.00
4,500	Continental Oil Co.	26,262.50	79,312.50
1,900	Canadian Pacific R. R. Co.	27,932.50	24,462.50
303	Electric Bond and Share Co.	5,935.00	3,636.00
500	General Electric Co.	6,525.00	9,750.00
200	Gulf Oil Co.	6,277.50	11,950.00
3,500	Great Northern R. R. Co.	61,732.50	68,687.50
500	Great Northern Iron Properties	3,925.00	5,500.00
100	International Harvester Co.	3,832.50	4,000.00
2,400	National Cash Register Co.	24,572.50	43,500.00
1,100	Northern Pacific R. R.	15,343.65	25,300.00
1,400	New York Central R. R. Co.	49,965.00	46,725.00
1,300	The Ohio Oil Co.	10,610.00	17,550.00
800	The Pennsylvania Railroad Co.	13,877.50	24,000.00
1,000	Royal Dutch Co.	14,175.00	36,000.00
500	Standard Oil Co. of Indiana	8,850.00	16,125.00
1,500	Standard Oil Co. of Kentucky	19,493.40	22,500.00
200	Socony Vacuum Oil Co.	1,977.50	3,250.00
400	Swift and Co.	6,670.00	5,700.00
300	Sears Roebuck and Co.	4,302.50	12,750.00
1,100	Standard Oil Co. of California	29,855.00	45,100.00
1,500	Southern Pacific R. R.	58,502.50	29,625.00
400	Simmons Co.	3,655.00	7,250.00
3,600	Shell Union Oil Co.	14,642.50	28,350.00
2,238	Transamerica Corp.	139,595.00	15,106.50
1,800	The Texas Corp.	23,340.00	43,875.00
500	Underwood Elliott Fisher Co.	12,380.00	18,750.00
200	U. S. Steel Corp.	9,140.00	9,550.00
200	Union Oil Associates	3,197.50	24,537.50
1,100	Union Oil Co. of California	23,515.00	
2,500	Weeden and Co.	100,000.00	70,000.00
		$782,190.55	$777,792.00

PETITIONER'S EXHIBIT 10

Wilson Bros. and Co.

STOCKS OF DOMESTIC CORPORATIONS

As at December 31, 1934

Number of Shares	Security	Cost	Approximate Market Value
200	A. T. & S. F. Railway	$ 13,320.00	$ 10,750.00
1,652	Byron Jackson Co.	13,168.50	11,977.00
400	Anglo National Corp.	21,000.00	2,650.00
4,500	Continental Oil Co.	26,262.50	84,937.50
2,600	Canadian Pacific R. R.	36,155.00	29,900.00
303	Electric Bond and Share Co.	5,935.00	2,272.50
900	General Electric Co.	13,520.00	20,025.00
200	Gulf Oil Co.	6,277.50	11,450.00
3,500	Great Northern R. R. Co.	61,732.50	59,500.00
500	Great Northern Iron Properties	3,675.00	6,000.00
300	International Harvester Co.	8,767.50	12,675.00
2,400	National Cash Register Co.	24,572.50	42,300.00
1,100	Northern Pacific R. R.	15,343.65	22,687.50
1,800	New York Central R. R. Co.	57,510.00	36,450.00
1,300	The Ohio Oil Co.	10,610.00	13,325.00
1,000	The Pennsylvania Railroad Co.	18,537.50	24,375.00
1,000	Royal Dutch Co.	14,175.00	29,250.00
500	Standard Oil Co. of Indiana	8,850.00	12,750.00
1,500	Standard Oil Co. of Kentucky	19,493.40	27,562.50
200	Socony Vacuum Oil Co.	1,977.50	2,950.00
400	Swift and Co.	6,670.00	7,600.00
300	Sears Roebuck and Co.	4,302.50	11,887.50
1,100	Standard Oil Co. of California	29,855.00	35,750.00
1,800	Southern Pacific R. R. Co.	63,480.00	32,400.00
400	Simmons Co.	3,655.00	4,000.00
3,600	Shell Union Oil Co.	14,642.50	25,200.00
2,238	Transamerica Corp.	139,595.00	13,148.25
1,800	The Texas Corp.	23,340.00	37,800.00
500	Underwood Elliott Fisher Co.	12,380.00	28,750.00
800	U. S. Steel Corp.	26,785.00	31,200.00
200	Union Oil Associates	3,197.50	31,750.00
1,800	Union Oil Co. of California	23,515.00	
200	Westinghouse Electric Co.	5,690.00	7,525.00
2,500	Weeden and Co.	100,000.00	80,000.00
	Unidentified difference	—212.50	none
		$837,778.05	$810,797.75

PETITIONER'S EXHIBIT 11

Wilson Bros. and Co.

BONDS OF DOMESTIC CORPORATIONS

As at Dates Shown Hereunder

Par Value	Security	January 1, 1932		December 31, 1932		December 31, 1933		December 31, 1934	
		Cost	Market Value	Cost	Market Value	Cost	Market Value	Cost	Market Value
$ 4,000.00	Union Oil Company of California, 1st lien s.f. 5/35	$ 3,975.00	$3,680.00	$ 3,975.00	$4,000.00	$ 3,975.00	$4,000.00	$ 3,975.00	$ 4,000.00
$18,000.00	Kentucky Fuel Gas Corporation, 1st lien s.f. 6½% A bonds due 1942	9,000.00	900.00	9,000.00		9,000.00		9,000.00	
15,000.00	Kentucky Fuel Gas Corporation, 1st lien s.f. 6½% A bonds due 1942			450.00	412.50	450.00	860.00	450.00	1,935.00
$33,000.00									
10,000.00	Kentucky Fuel Gas Corporation, 1st lien s.f. 6½% A bonds due 1942					20.00		20.00	
$43,000.00									
$16,000.00	New York Central R. R.							16,800.00	18,800.00
	Totals	$12,975.00	$4,580.00	$13,425.00	$4,412.50	$13,445.00	$4,860.00	$30,245.00	$24,735.00
	Deduct:								
	Charge to 1934 income in respect of partial worthlessness of Kentucky Fuel Gas Corp. debentures							5,500.00	
		$12,975.00	$4,580.00	$13,425.00	$4,412.50	$13,445.00	$4,860.00	$24,745.00	$24,735.00

PETITIONER'S EXHIBIT 18

Wilson Bros. and Co.

GENERAL LEDGER TRIAL BALANCES

(After Closing)

	January 1, 1932		December 31, 1932		December 31, 1933		December 31, 1934	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Bank of America, Los Angeles	$ 259.79						$ 52,149.82	
Crocker First National Bank		$ 25.25	$ 23,989.81		$ 539.04		142.48	
The San Francisco Bank	403,750.00		51,324.00					
Wells Fargo Bank	320.83		21,324.42		8,647.39		21,415.06	
Capital		2,500,000.00		$2,500,000.00		$2,500,000.00		$2,535,000.00
Surplus		12,792.64		19,309.75		36,732.00		25,447.64
Treasury stock	250,000.00		250,000.00		250,000.00		250,000.00	
Treasury stock								10,000.00
Capital stock tax account						400.00		
Bond	12,975.00		13,425.00		13,425.00		7,925.00	
Bond Trading					20.00		16,820.00	
Merchandise	20,942.18				6,500.00		3,946.60	
Auto account	5,400.00		4,500.00		2,850.15		1,200.30	
Sales tax								1,188.06
Furniture and fixtures	3,500.00		3,000.00		2,500.00		2,000.00	
Reserve bad accounts						2,160.80		6,884.90
Real estate	47,000.00		46,000.00		45,000.00		44,500.00	
S. S. Idaho	56,250.00		52,500.00		45,000.00		41,250.00	
S. S. Oregon	75,000.00		70,000.00		60,000.00		55,000.00	
Str. Svea	6,420.36		9,081.78		10,804.01		12,861.01	
Str. Idaho minority interest		3,409.11		3,064.68		2,378.71		2,058.33
Str. Svea							350.00	
Atchison, Topeka & Santa Fe R. R.			13,320.00		17,940.00		13,320.00	
Anglo Natl. Corp	21,000.00		21,000.00		21,000.00		21,000.00	
Byron Jackson Co.			13,168.50		13,168.50		13,168.50	
Canadian Pacific R. R. Co.	16,257.50		27,932.50		27,932.50		36,155.00	
Continental Oil Co.	1,842.50		26,262.50		26,262.50		26,262.50	
Call loans			100,000.00		151,000.00		171,000.00	
Electric Bond & Share Co.	4,937.50		5,935.00		5,935.00		5,935.00	
Economy Lumber Co.					152.43			
General Electric Co.					6,525.00		13,520.00	
Gulf Oil Co.	3,307.50		6,277.50		6,277.50		6,277.50	
Great Northern R. R. Co.	23,362.50		61,732.50		61,732.50		61,732.50	
Great Northern Iron Properties					3,925.00		3,675.00	
International Harvester Co.	3,832.50		3,832.50		3,832.50		8,767.50	
The National Cash Register Co.	9,752.50		24,572.50		24,572.50		24,572.50	
Northern Pacific R. R. Co.	4,952.50		12,807.50		15,343.65		15,343.65	
New York Central R. R. Co.	27,495.00		49,965.00		49,965.00		57,510.00	
The Ohio Oil Co.	3,650.00		10,610.00		10,610.00		10,610.00	
The Pennsylvania Railroad Co.	9,250.00		13,877.50		13,877.50		18,537.50	
Royal Dutch Co.	2,722.50		14,175.00		14,175.00		14,175.00	
(Forward)	$1,014,180.66	$2,516,227.00	$ 950,613.51	$2,522,374.43	$ 919,512.67	$2,541,671.51	$1,031,122.42	$2,580,578.93

PETITIONER'S EXHIBIT 18
(Continued)
Wilson Bros. and Co.

GENERAL LEDGER TRIAL BALANCES
(After Closing)

	January 1, 1932		December 31, 1932		December 31, 1933		December 31, 1934	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
(Forwarded)	$1,014,180.66	$2,516,227.00	$ 950,613.51	$2,522,374.43	$ 919,512.67	$2,541,671.51	$1,031,122.42	$2,580,578.93
Standard Oil Co. of Indiana	8,850.00		8,850.00		8,850.00		8,850.00	
Standard Oil Co. of Kentucky	9,872.50		18,495.00		19,493.40		19,493.40	
Socony Vacuum Oil Co.	1,977.50		1,977.50		1,977.50		1,977.50	
Swift & Co.					6,670.00		6,670.00	
Sears, Roebuck & Co.					4,302.50		4,302.50	
Standard Oil Co. of Calif.	24,905.00		29,855.00		29,855.00		29,855.00	
Southern Pacific R. R. Co.	44,342.50		58,502.50		58,502.50		63,480.00	
Simmons Company	3,655.00		3,655.00		3,655.00		3,655.00	
Shell Union Oil Co.	9,242.50		14,642.50		14,642.50		14,642.50	
Transamerica Corp.	139,595.00		139,595.00		139,595.00		139,595.00	
The Texas Corporation	12,165.00		23,340.00		23,340.00		23,340.00	
Underwood Elliott Fisher Co.	10,862.50		12,380.00		12,380.00		12,380.00	
U. S. Steel Corp.					9,140.00		26,785.00	
Union Oil Associates	3,197.50		3,197.50		3,197.50		3,197.50	
United Fruit Co.			7,470.00					
Union Oil Co.	15,642.50		23,515.00		23,515.00		23,515.00	
Weeden & Co.	100,000.00		100,000.00		100,000.00		100,000.00	
Westinghouse Electric Co.							5,690.00	
Bills receivable			14,000.00					
Associated Lumber Co.							969.42	
Angelus Lumber Co.	90.00		531.34					
Columbia Studio, Inc.							800.79	
Ellis Bros. Lumber Co.	761.35		331.35					
Exposition Lumber Co.					107.50		142.50	
Dolan Wrecking & Constr. Co.	684.30		664.12					
Fox Film Corp.							8,918.43	
General Mill & Lumber Co.	82.80		82.80					
Gorden Mill & Supply Co.	547.92		349.36					
Glick Bros. Sash & Door	447.76							
Giles Lumber Co.			40.42					
Hayman Bldg. Supply Co.			25.00					
Phil Hart Lumber Co.	1,128.04		1,128.04					
Herzog Lumber & Door Co.	591.61				3,800.90		734.69	
Hubner Lumber Co.			137.73		140.00			
Hudson-Bowney Lumber Co.							134.81	
T. P. Hogan Co.	100.00		100.00					
Huff Lumber Co.					687.50			
Imperial Lumber Co.	271.16		216.50		1,501.89		1,005.69	
(Forward)	$1,403,193.10	$2,516,227.00	$1,413,695.17	$2,522,374.43	$1,384,866.36	$2,541,671.51	$1,531,257.15	$2,580,578.93

PETITIONER'S EXHIBIT 18
(Continued)
Wilson Bros. and Co.

GENERAL LEDGER TRIAL BALANCES
(After Closing)

	January 1, 1932		December 31, 1932		December 31, 1933		December 31, 1934	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
(Forwarded)	$1,403,193.10	$2,516,227.00	$1,413,695.17	$2,522,374.43	$1,384,866.36	$2,541,671.51	$1,531,257.15	$2,580,578.93
Johnson Lumber Co.					402.50			
Lucas Manufacturing Co.	800.00		800.00					
Murphy Lumber Co.							632.26	
Pico Lumber Co.							2,672.07	
Paramount Productions							804.23	
Read-Pratt Co.	899.41		899.41					
E. M. Strawn Lumber Co.							227.41	
Southwestern Lumber Co.	310.39		242.21				185.78	
R. K. O. Studios, Inc.							215.03	
Karl Rohberg			500.00		500.00		500.00	
Peninsula Lumber Co.	195.00		182.87					
Valley Salvage Co.							162.89	
Ventura Wrecking Co.	721.23		721.23					
H. A. Van Der Top					28.24			
Woodhead Lumber Co.—Calif.	47,036.19		44,368.96		43,276.06		37,145.76	
Woodhead Lumber Co.—Nevada			11,594.97		33,422.98		32,494.49	
W. Wilson	17,717.88		17,717.88		16,917.88		16,917.88	
F. A. Wilson		15,000.00			28,091.96		35,612.50	
Mrs. H. Wilson	17,132.40	1,000.00	21,248.51		21,128.51		21,128.51	
Warner Bros.							2,395.34	
Stanger Lumber Co.	159.22							
Mel Coe Lumber Co.	350.00		114.36					
Inglewood Lumber Co.	365.32							
Hyman Bldg. Co.	25.00							
J. R. Duffield & Co.	75.00							
	$1,488,980.14	$2,532,227.00	$1,512,085.57	$2,522,374.43	$1,528,634.49	$2,541,671.51	$1,682,351.30	$2,580,578.93

PETITIONER'S EXHIBIT 19

Wilson Bros. and Co.

ACCOUNTS RECEIVABLE

January 1, 1932

Angelus Lumber Co.	$ 90.00
Ellis Bros. Lumber Co.	761.35
Dolan Wrecking and Construction Co.	684.30
General Mill and Lumber Co.	82.80
Garden Mill and Supply Co.	547.92
Glick Bros. Sash and Door Co.	447.76
Phil Hart Lumber Co.	1,128.04
Herzog Lumber and Door Co.	591.61
T. P. Hogan Co.	100.00
Imperial Lumber Co.	271.16
Lucas Manufacturing Co.	800.00
Read-Pratt Co.	899.41
Southwestern Lumber Co.	310.39
Peninsula Lumber Co.	195.00
Ventura Wrecking Co.	721.23
Woodhead Lumber Co.	47,036.19
Stangor Lumber Co.	159.22
Mel Coe Lumber Co.	350.00
Inglewood Lumber Co.	365.32
Hyman Bldg. Co.	25.00
J. R. Duffield & Co.	75.00
Atlantic Lumber Co.	45.00
Fisher Co.	35.00
E. F. Hutton Co.	5,173.99
S. S. Svea	6,420.36
	$67,316.05

PETITIONER'S EXHIBIT 20

Wilson Bros. and Co.

ACCOUNTS RECEIVABLE

December 31, 1932

Atlantic Lumber Co.	$ 462.13
Angelus Lumber Co.	531.34
Ellis Bros. Lumber Co.	331.35
Dolan Wrecking and Construction Co.	664.12
General Mill and Lumber Co.	82.80
Garden Mill and Supply Co.	349.36
Giles Lumber Co.	40.42
Hayman Building Supply Co.	25.00
Phil Hart Lumber Co.	1,128.04
Hubner Lumber Co.	137.73
T. P. Hogan Co.	100.00
Imperial Lumber Co.	216.50
Lucas Manufacturing Co.	800.00
Read-Pratt Co.	899.41
Southwestern Lumber Co.	242.21
Karl Rohberg	500.00
J. C. Smith Lumber Co.	87.89
Peninsula Lumber Co.	182.87
Mel Coe Lumber Co.	114.36
Ventura Lumber Co.	721.23
Woodhead Lumber Co. of California	44,368.96
Woodhead Lumber Co. of Nevada	11,594.97
S. S. Svea	9,081.78
	$72,662.47

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PETITIONER'S EXHIBIT 21

Wilson Bros. and Co.

ACCOUNTS RECEIVABLE

December 31, 1933

Advance Lumber Co.	$ 100.00
Economy Lumber Co.	152.43
Exposition Lumber Co.	107.50
Herzog Lumber and Door Co.	3,800.90
Hubner Lumber Co.	140.00
Huff Lumber Co.	687.50
Imperial Lumber Co.	1,501.89
Johnson Lumber Co.	402.50
Karl Rohberg	500.00
H. A. Van der Top	28.24
Woodhead Lumber Co. of California	43,276.06
Woodhead Lumber Co. of Nevada	33,422.98
S. S. Svea	10,804.01
	$94,924.01

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PETITIONER'S EXHIBIT 22

Wilson Bros. and Co.

ACCOUNTS RECEIVABLE

December 31, 1934

Associated Lumber Co.	$ 969.42
Columbia Studio, Inc.	800.79
Exposition Lumber Co.	142.50
Fox Film Corp.	8,918.43
Herzog Lumber and Door Co.	734.69
Hudson-Bowney Lumber Co.	134.81
Imperial Lumber Co.	1,005.69
Murphy Lumber Co.	632.26
Pico Lumber Co.	2,672.07
Paramount Productions	804.23
E. M. Strawn Lumber Co.	227.41

Southwestern Lumber Co.	185.78
R. K. O. Studios, Inc.	215.03
Karl Rohberg	500.00
Valley Salvage Co.	162.89
Woodhead Lumber Co. of California	37,145.76
Woodhead Lumber Co. of Nevada	32,494.49
S. S. Svea	12,861.01
Warner Bros.	2,395.34
	$103,002.60

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PETITIONER'S EXHIBIT 23

Wilson Bros. and Co.

ACCOUNTS RECEIVABLE—F. A. WILSON

Charges—1933:			
April	26—Proceeds sale of Great Northern Pfd. and other shares	$17,112.50	
May	31—Profit on General Electric Company shares traded	437.00	
	31—Proceeds sale of Simmons Co., and other shares	28,516.25	
June	20—Proceeds sale of General Electric Co., shares	2,471.00	
July	30—Proceeds sale of United Fruit Co. shs.	19,185.75	
	1—Proceeds sale of General Electric Co. shares	3,377.37	
	20—Proceeds sale of A. T. & S. F. Ry. shs.	608.50	
	24—Proceeds sale of International Harvester Co. shares	10,113.00	
Nov.	8—Profit on U. S. Steel Corp. traded	776.40	$ 82,597.77

Credits—1933:			
July	24—Borrowing tax on United Fruit Co. shares	8.40	
Oct.	14—Deposit Wells Fargo Bank account of Wilson Bros. and Co.	15,000.00	
Oct.	20—	3,925.00	
Sept.	27—Purchase Swift and Co.	6,670.00	
Dec.	30—Purchase of U. S. Steel Corp. shs.	13,760.00	39,363.40
Due from F. A. Wilson December 31, 1933			$ 43,234.37
Charges—1934:			
Jan.	29—Proceeds sale of U. S. Steel Corp. shares	17,454.60	
Sept.	15—	100.00	
Oct.	15—	30.00	
Oct.	23—	60.00	
Nov.	27—Cash paid by Wilson Bros. and Co.	4,607.50	
Nov.	9—Cash paid by Wilson Bros. and Co.	2,581.03	
Dec.	22—Cash paid by Wilson Bros. and Co.	19,368.75	
Dec.	14—Cash paid by Wilson Bros. and Co.	17,997.50	62,199.38
			$105,433.75
Credits—1934:			
July	26—Purchase U. S. Steel Corp. shs.	$55,940.00	
Oct.	30—Purchase U. S. Steel Corp. shs.	6,340.00	
Nov.	5—Purchase Canadian Pac. Rd. shs.	1,180.00	
Nov.	21—Purchase Canadian Pac. Rd. Shs.	4,607.50	
Dec.	20—Purchase Southern Pac. Co. shs.	1,742.50	
Dec.	30—Shipping charges on shares	11.25	69,821.25
Due from F. A. Wilson December 31, 1934			$ 35,612.50
Credits—1935:			
Jan.	2—Purchase of Kennecott Copper Co. and other shares		35,612.50

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EX. "A" 150

RESPONDENT'S EXHIBIT "A"

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Form 1120
TREASURY DEPARTMENT
Internal Revenue Service
(Collector's Stamp)

CORPORATION INCOME TAX RETURN
For Calendar Year 1929

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1930

Page 1 of Return

File No. 781

Serial Number 661856

(Collector's Stamp)

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

Wilson Bros. & Co.
(Name)

1312 Russ Building
(Street and number)

San Francisco, California.
(Post office and State)

Cash Check M.O. Date of Ind. Pay. Payment

Date of Incorporation December 14, 1928.

Under the Laws of what State or Country Nevada

Kind of Business

Is This a Consolidated Return of Two or More Corporations?

	GROSS INCOME			
1.	Gross Sales from Trading or Manufacturing, Less Returns and Allowances		$353 633 46	
2.	Less Cost of Goods Sold:			
	(a) Inventory at beginning of year	$		
	(b) Merchandise bought for sale	349 215 83		
	(c) Cost of manufacturing or producing goods (From Schedule A)			
	(d) Total of lines (a), (b), and (c)	$ 349 215 83		
	(e) Less inventory at end of year	43 140 00	306 075 83	
3.	Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)		$47 757 63	
4.	Gross Profit from Operations Other Than Trading or Manufacturing (State nature of business)			
	(a) Management		2 865 81	
	(b)			
	(c)			
5.	Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds		6 445 02	
6.	Rents		1 080 00	
7.	Royalties			
8.	Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule B)			
9.	Dividends on Stock of Domestic Corporations		12 159 00	
10.	Other Income (including dividends received on stock of foreign corporations). (State nature of business)			
	(a)			
	(b)			
	(c)			
11.	TOTAL INCOME IN ITEMS 3 TO 10			$ 70 297 46
	DEDUCTIONS			
12.	Compensation of Officers (From Schedule C)	$		
13.	Rent on Business Property		2 280	
14.	Repairs (From Schedule D)			
15.	Interest			
16.	Taxes (From Schedule E)		292 22	
17.	Losses (From Schedule F)			
18.	Bad Debts (From Schedule G)			
19.	Dividends (From Schedule H)		12 159	
20.	Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule I)		19 498 75	
21.	Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see instruction 21)			
22.	Other Deductions Not Reported Above. (Explain below, or on separate sheet) Steamer Operation		11 781 51	
	(a) Salaries and wages. (Not included in Item 3, 12, or 14 above)		14 580 00	
	(b) Net Loss for prior year (Submit schedule) Miscellaneous Expense		9 649 46	
	(c)			
	(d)			
	(e)			
	(f)			
23.	TOTAL DEDUCTIONS IN ITEMS 12 TO 22			$ 70 240 74
24.	NET INCOME (Item 11 minus Item 23)			$ 56 72

COMPUTATION OF TAX

25. Net Income (Item 24 above)	$	28. Income Tax (12% of Item 27)	$
26. Less Credit of $3,000 (for a domestic corporation having a net income of less than $25,360)		29. If net income of domestic corporation is less than $25,360, enter the amount over $25,000	
27. Balance (Item 25 minus Item 26)	$	30. Total Tax (Item 28 plus Item 29)	$
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)		$	
32. Income Tax Paid to a Foreign Country or U. S. possession by a domestic corporation (see Inst. 27)			
33. Balance of Tax (Item 30 minus Items 31 and 32)			$

An amended return must be marked "Amended" at top of return.

Checks and drafts will be accepted only if payable at par

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Page 2 of Return — SCHEDULE E—BALANCE SHEETS (See Instruction 6)

Items	Beginning of Taxable Year		End of Taxable Year	
	Amount	Total	Amount	Total
ASSETS				
1. Cash		$ 200 000 00		$ 151 175 45
2. Notes receivable				4 785 02
3. Accounts receivable	$		$ 61 968 46	
Less reserve for bad debts				61 968 46
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods			43 140	
Supplies				
				43 140 ✓
5. Investments (nontaxable):				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Securities issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Other investments:				
Stocks of domestic corporations	$ 466 000		$ 486 000	
Bonds of domestic corporations				
Stocks and bonds of foreign corporations				
All other investments or loans	175 000	641 000 ✓	157 500	643 500
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
All other				
8. Capital assets:				
Land		30 000		30 000
Buildings	$ 20 000		$ 20 000	
Machinery and equipment			5 000	
Furniture and fixtures	5 000		5 000	
Delivery equipment				
	$ 25 000		$ 30 000 ✓	
Less reserves for depreciation		25 000 ✓	1 500	28 500 ✓
9. Patents				
10. Good will				
11. Other assets (describe fully):				
	$		$	
12. TOTAL ASSETS		$ 896 000		$ 963 056 91 ✓
LIABILITIES				
13. Notes payable (less than one year)		$ 200 000		$ 200 000
14. Accounts payable				4 841 19
15. Bonds and notes (not secured by mortgage)				
16. Mortgages (including bonds and notes so secured)				
17. Accrued expenses:				
Interest	$		$	
Taxes				
All other				
18. Other liabilities (describe fully):				
19. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)		696 000	746 000	746 000 ✓
20. Surplus	$		$	
21. Undivided profits				12 213 72
22. TOTAL LIABILITIES		$ 896 000		$ 963 056 91 ✓

Remarks

Form

SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 30, page 1 of the return					56	72	1. Unallowable deductions:			
2. Nontaxable income:							(a) Income, war, and excess-profits taxes			
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia							(b) Dividends and profits taxes paid to the United States, and so much of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of the return			
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended							(c) Federal taxes paid on tax-free covenant bonds			
(c) Interest on obligations of the United States or its possessions							(d) Special improvement taxes locating or increasing the value of the property assessed			
(d) Dividends deductible under Section 28(p) of the Revenue Act of 1928			12	159	00		(e) Furniture and fixtures, additions, or betterments treated as expenses on the books			
(e) Proceeds of life insurance policies paid upon the death of the insured							(f) Replacements and renewals			
(f) Other items of nontaxable income (to be detailed):							(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary			
(1)							(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation			
(2)							(i) Additions to reserves for bad debts which are not included in Item 18, page 1 of return			
(3)							(j) Additions to reserves for contingencies, etc. (to be detailed):			
3. Charges against reserve for bad debts, if Item 18, page 1 of return, is not an addition to a reserve							(1)			
4. Charges against reserves for contingencies, etc. (to be detailed):							(2)			
(a)							(3)			
(b)							(k) Other unallowable deductions (to be detailed):			
(c)							(1)			
5. Total of Lines 1 to 4, inclusive			12	215	72		(2)			
6. Total from Line 14			12	215	72		(3)			
7. Net profit for year, as shown by books, before any adjustments are made thereon (Line 5 minus Line 6)			12	215	72		14. Total of Line 13			
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year			12	215	72		15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):			
9. Other credits to surplus (to be detailed):							(a) Date paid ..... Character			
(a)							(b) Date paid ..... Character			
(b)							(c) Date paid ..... Character			
(c)							(d) Date paid ..... Character			
10. Total of Lines 7 to 9, inclusive							16. Other debits to surplus (to be detailed):			
11. Total from Line 17							(a)			
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)			12	215	72		(b)			
							(c)			
							17. Total of Lines 15 and 16			

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, including fishing, logging, ice harvesting, etc., and also the leasing of such property. State the product or products. B.—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C.—Manufacturing. State the product and also the material if not implied by the name of the product. D.—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. E1.—Transportation—rail, water, local, etc. State the kind and special product transported, if any. E2.—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. E3.—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. E4.—Leasing transportation or utilities. State kind of property. F.—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Sales with storage with profit primarily from sales. G.—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. H.—Finance, including banking, real estate, insurance. I.—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the same product is concerned, should report business so identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers:

(a) General class (use key letter designation) F

(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)

Lumber and Shipping

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION H

4. Is this a consolidated return of two or more corporations? No

If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filed in, cover, and filed as a part of this return. See Article 12 (c) and (d), Regulations 75.

5. Did the corporation file a consolidated return for the preceding taxable year? No

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? No Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? If answer is "yes," give name and address of each predecessor business, and the date of the change in entity.

Upon such change were any asset values increased or decreased? If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of actual receipts and disbursements? Yes If not, describe fully what other basis or method was used in computing net income.

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock.

Cost

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

The corporation's books are in care of

Located at 1512 Russ Building, San Francisco, Cal.

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Schedule A—Cost of Manufacturing or Producing Goods

[Not filled in]

Schedule B

Profit from Sale of Real Estate, Stocks, Bonds, etc.

[Not filled in]

Schedule C—Compensation of Officers

[Not filled in]

Schedule D—Cost of Repairs

[Not filled in]

Schedule E—Taxes Paid

[Not filled in]

Schedule F—Explanation of Losses by Fire, Storm, etc.

[Not filled in]

Schedule G—Bad Debts

[Not filled in]

Schedule H—Dividends Deductible

[Not filled in]

Schedule I—Explanation of Deduction for Depreciation

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquirement	5. Cost or Value as of March 1, 1913, Whichever Greater (Exclusive of Land)	Amount of Depreciation Charged Off	
					6. Previous Year	7. This year
Wooden Building	Jan. 2, 1929			$ 20000	$	$ 1000
" Steamers	"	10 years	10 years	175000		17500
Automobile	May 1930	New		5498.75		498.75
Furniture	Jan. 2, 1929		10 years	5000		500
					[In pencil]	19498.75

Affidavit

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

[Corporate Seal] T. A. WILSON
President
W. T. WILSON
Treasurer.

Sworn to and subscribed before me this 15th day of March, 1930.

[Notarial Seal] JOHN J. MAY, DO

Attach a separate sheet if any of the above schedules do not provide sufficient space.

[Endorsed]: Respondent's Exhibit A. Admitted in evidence June 7, 1939. [159]

EXHIBIT "F"

RESPONDENT'S EXHIBIT "B"

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Form 1120
TREASURY DEPARTMENT
Internal Revenue Service
(Auditor's Stamp)

CORPORATION INCOME TAX RETURN
For Calendar Year 1930

Page 1 of Return

File No.

Serial Number

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1931

PRINT PLAINLY CORPORATION'S NAME AND BUSINESS ADDRESS

District (Collector's Stamp)

Name: Pure Oil Bldg
Office and Street: San Francisco

Date of Incorporation: Dec 14 1928

Under the Laws of what State or Country: Nevada

Cash Check M. O. Cert. of Ind. Final Payment

Kind of Business: Towing & Shipping

Is This a Consolidated Return of Two or More Corporations? No. If so, How Many?

Item not taxable by

GROSS INCOME

1. Gross Sales from Trading or Manufacturing, $	Less Returns and Allowances, $	Net Sales, $	139 19614
2. Less Cost of Goods Sold			
(a) Inventory at beginning of year		$	43 14000
(b) Merchandise bought for sale			122 67142
(c) Cost of manufacturing or producing goods (From schedule A) Salaries and Wages, $; Other costs, $; Total			
(d) Total of lines (a), (b), and (c)		$	165 81142
(e) Less inventory at end of year			38 53942
			127 28200
3. Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)		$	11 91414
4. Gross Profit from Operations Other Than Trading or Manufacturing (State nature of income)			
(a)			
(b) Managment Steamer			919 33
(c)			
5. Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds			783383
6. Rents			10800
7. Royalties			
8. Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From schedule B)			
9. Dividends on Stock of Domestic Corporations			17 13055
10. Other Income (including dividends received on Stock of foreign corporations) (State nature of income)			
(a)			
(b)			
(c)			
11. Total Income (Items 3 to 10)		$	38 91785

DEDUCTIONS

12. Compensation of Officers (From schedule C)	$	
13. Rent on Business Property		23 9400
14. Repairs (From schedule D), Salaries and Wages, $; Other Costs, $; Total		
15. Interest		
16. Taxes (From schedule E)		10 7436
17. Losses (From schedule F) Steamer Operation		38 5360
18. Bad Debts (From schedule G)		
19. Dividends (From schedule H)		17 13055
20. Depreciation (resulting from exhaustion, wear and tear or obsolescence) (From schedule I)		20 4505 0
21. Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction H)		
22. Other Deductions Not Reported Above (Explain below or on separate sheet) Misc. Expense		53 4952
(a) Salaries and wages (Not included in Item 5, 12, or 14 above)		11 4600
(b) Net Loss for 1928-1929 (Submit schedule)		
(c)		
(d)		
(e)		
23. Total Deductions (Items 12 to 22)	$	6 18 2053
24. Net Income (Item 11 minus Item 23)	$	32 72732

COMPUTATION OF TAX

25. Net Income (Item 24 above)	$	26. Income Tax (12% of Item 27)	$
26. Less Credit of $3,000 (for a domestic corporation having a net income of less than $25,000)		29. If net income of domestic corporation is less than $25,000, enter the amount over $25,000	
27. Balance (Item 25 minus Item 26)	$	30. Total Tax (Item 28 plus Item 29)	$
31. Less: Income Tax Paid at Source. (This credit can only be allowed to a nonresident foreign corporation)	$		
32. Income Tax Paid to a Foreign Country or U. S. possession by a domestic corporation (see Inst. 27)			
33. Balance of Tax (Item 30 minus Items 31 and 32)			$

An amended return must be marked "Amended" at top of return. Checks and drafts will be accepted only if payable at par

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Page 3 of Return — SCHEDULE E. BALANCE SHEETS (See Instructions 43)

Item	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
ASSETS				
1 Cash		177343		56597357
2 Notes receivable		468502		
3 Accounts receivable	8185846	8185846	20062399	20062399
Less reserve for bad debts				
4 Inventories				
Raw materials				
Work in process				
Finished goods	43140		3852942	
Supplies				
		43140		3852942
5 Investments (nontaxable)				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia				
Securities issued under the Federal Farm Loan Act or under such Act as amended				
Obligations of the United States or its possessions				
6 Other investments				
Stocks of domestic corporations	486000		50458500	
Bonds of domestic corporations			1197500	
Stocks and bonds of foreign corporations				
All other investments of bonds	157500	643500	14000000	65657000
7 Deferred charges				
Prepaid insurance				
Prepaid taxes				
All other				
8 Capital assets		30000		30000
Land	20000		20000	
Buildings	6800		775850	
Machinery and equipment	5000		5000	
Furniture and fixtures				
Delivery equipment				
	30000		3275850	
Less reserves for depreciation	1500	28500	445850	28300
9 Patents				
10 Good will				
11 Other assets (describe fully)				
12 Total Assets		9630691		101067699
LIABILITIES				
13 Notes payable (less than one year)		300000		200000
14 Accounts payable		484119		4165540
15 Bonds and notes (not secured by mortgage)				
16 Mortgages (including bonds and notes so secured)				
17 Accrued expenses				
Interest				
Taxes				
All other				
18 Other liabilities (describe fully)				
19 Capital stock				
Preferred stock (less stock in treasury)				
Common stock (less stock in treasury)	746000	746000	74000	800000
20 Surplus				
21 Undivided profits		122571		6456159
22 Total Liabilities		9630691		101067699

Remarks

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SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from Item 30, page 1 of the return		22894	69	Deductions allowable: (a) Depreciation, depletion, and amortization				
2. Nontaxable income: (a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia				(b) Income and profits taxes paid to the United States, and on account of such taxes paid to its possessions or foreign countries as are claimed as a credit in Item 32, page 1 of this return				
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended				(c) Federal taxes paid on tax-free covenant bonds				
(c) Interest on obligations of the United States or its possessions		17	3055	(d) Special improvement taxes tending to increase the value of the property assessed				
(d) Dividends deductible under Section 28(p) of the Revenue Act of 1918				(e) Furniture and fixtures, additions, or betterments treated as expenses on the books				
(e) Proceeds of life insurance policies paid upon the death of officers or employees, if not included in gross income				(f) Replacements and renewals				
(f) Other items of nontaxable income (to be itemized): (1)				(g) Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary				
(2)				(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation				
(3)				(i) Additions to reserve for bad debts which are not included in Item 16, page 1 of return				
3. Charges against reserve to be included in Item 5, page 1 of return, which is not an addition to it				(j) Additions to reserves for contingencies, etc. (to be itemized): (1)				
4. Charges against reserves not shown in Item 5 (to be itemized): (a)				(2)				
(b)				(3)				
(c)				(k) Other unallowable deductions (to be itemized): (1)				
5. Total of Lines 1 to 4, inclusive		5764	13	(2)				
6. Income for the year (Line 5 less Line 2)				(3)				
7. Surplus at beginning of year, as shown by books, before any adjustments are made thereto (Line 4 minus Line 6)				14. Total of Line 13				
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year		12	2457	15. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property): (a) Date paid ... Character ...				
Other credits to surplus (to be itemized): (a)				(b) Date paid ... Character ...				
(b)				(c) Date paid ... Character ...				
(c)				(d) Date paid ... Character ...				
10. Total of Lines 7 to 9, inclusive				16. Other debits to surplus (to be itemized): (a)				
11. Total from Line 17				(b)				
12. Surplus and undivided profits as shown by balance sheet at close of taxable year (Line 10 minus Line 11)		6457	85	(c)				
				17. Total of Lines 13 and 16				

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special description of the business sufficient to give the information called for under each general class.

A.—Agriculture and related industries, (including fishing, logging, tea harvesting, etc., and also the leasing of such property. State the product or products. **B.**—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. **C.**—Manufacturing. State the product and also the material if not implied by the name of the product. **D.**—Construction—excavations, buildings, bridges, railroads, ships, etc., also equipping and installing same with systems, devices, or machinery, without their manufacture. State nature of structures built, materials used, or kind of installations. **E1.**—Transportation—rail, water, local, etc. State the kind and special product transported, if any. **E2.**—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. **E3.**—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. **E4.**—Leasing transportation or utilities. State kind of property. **F.**—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled Sales with storage with profit primarily from sales. **G.**—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or technical service. State the service. **H.**—Finance, including banking, real estate, insurance. **I.**—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the *same product* is concerned, should report business as identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E1 or E2 may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answers
(a) General class (use key letter designation) F
(b) Main income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 38

4. Is this a consolidated return of two or more corporations? No
If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed as a part of this return. See Article 12 (c) and (d), Regulations 75.

5. Did the corporation file a consolidated return for the preceding taxable year? ...

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? No. Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? ... If answer is "yes," give name and address of each predecessor business, and the date of the change in entity. ...

Upon such change were any asset values increased or decreased? ...
If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of actual receipts and disbursements? Yes
If not, describe fully what other basis or method was used in computing net income. ...

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with stock. Cost

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

The corporation's books are in care of ...
Located at Main Bldg. D.F. ...

Page 4 of Return

SCHEDULE A—COST OF MANUFACTURING OR PRODUCING GOODS (See Instruction 9)

Items	Amount	Items	Amount (Enter on Line 10)
Salaries and wages	$		$
Material and supplies			

SCHEDULE B—PROFIT FROM SALE OF REAL ESTATE, STOCKS, BONDS, ETC. (See Instruction 6)

1. Kind of Property	2. Date Acquired	3. Amount Received	4. Depreciation Allowable Since Acquisition	5. Cost or Value as of March 1, 1913, Whichever Obtained	6. Depreciation Allowable	7. Net Profit (Enter on Line 6)
		$	$	$	$	$

State how property was acquired

SCHEDULE C—COMPENSATION OF OFFICERS (See Instruction 12)

1. Name of Officer	2. Official Title	3. Time Devoted to Business	Shares of Stock Owned: 4. Common	4. Preferred	5. Amount of Compensation (Enter on Line 11)
					$

SCHEDULE D—COST OF REPAIRS (See Instruction 14)

1. Items	2. Amount (Enter on Line 16)
Salaries and wages	$

SCHEDULE E—TAXES PAID (See Instruction 16)

1. Items	2. Amount (Enter on Line 18)
	$

SCHEDULE F—EXPLANATION OF LOSSES BY FIRE, STORM, ETC. (See Instruction 17)

1. Kind of Property	2. Date Acquired	3. Cost or Value as of March 1, 1913, Whichever Obtained	4. Subsequent Improvements	5. Depreciation Allowable Since Acquisition	6. Insurance and Salvage Value	7. Deductible Loss (Enter on Line 19)
		$	$	$	$	$

State how property was acquired

SCHEDULE G—BAD DEBTS (See Instruction 18)

1. Year	2. Basis on Account	3. Bad Debts
1926	$	$
1927		
1928		
1929		
1930		

SCHEDULE H—DIVIDENDS DEDUCTIBLE (See Instruction 19)

1. Name of Corporation	Amount of Dividends: 2. Domestic	3. Foreign
	$	$

SCHEDULE I—EXPLANATION OF DEDUCTION FOR DEPRECIATION (See Instruction 20)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Age When Acquired	4. Probable Life After Acquisition	5. Cost or Value as of March 1, 1913, Whichever Obtained (Exclusive of Land)	Amount of Depreciation Claimed for: 6. Previous years	7. This year
Wooden Bldg	Jan 1911		20 years	$ 2000	$ 1000	$ 1000
" Stockers	"	10 years	10 "	1750 00	1750 00	
Furniture	"		10 "	500	500	
Auto	1929	new		5492 25	492 25	1000
"	1930	"		2750 00		450 00

AFFIDAVIT 1930 $ 2049 25

We, the undersigned, president and treasurer of the corporation for which this return is made, being severally duly sworn, each for himself, declare that this return, including the accompanying schedules and statements, has been examined by him and is, to the best of his knowledge and belief, a true and complete return made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1928 and the Regulations issued thereunder.

Sworn to and subscribed before me this 16 day of March, 1931

G. A. Wilson, President

W. T. Wilson, Treasurer

Attach a separate sheet if any of the above schedules do not provide sufficient space

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EXHIBIT "C" 54

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RESPONDENT'S EXHIBIT "C"

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Form 1120
TREASURY DEPARTMENT
Internal Revenue Service
(Collector's Stamp)

CORPORATION INCOME TAX RETURN
For Calendar Year 1931

File This Return with the Collector of Internal Revenue for Your District on or Before March 15, 1932

Page 1 of Return

File No. 781

Serial Number 854923

District 1 Calif.
(Collector's Stamp)

REVIEWED
SECTION E

PRINT PLAINLY Corporation's Name and Business Address

WILSON BROS. & Co.
(Name)

1518 Rose Building, 235 Montgomery St.
(Street and Number)

San Francisco, California.
(Post office and State)

Date of Incorporation December 14, 1928

Under the Laws of what State or Country Nevada

Cash Check M.O. Cert. of Int. First Payment

$

Kind of Business Wholesale merchants Is This a Consolidated Return of Two or More Corporations? ____ If so, How Many? ____

Item No.									
	GROSS INCOME								
1.	Gross Sales from Trading or Manufacturing, $ ____ Less Returns and Allowances, $ ____ ; Net Sales						$	64 346 56	
2.	Less Cost of Goods Sold:								
	(a) Inventory at beginning of year			20 529 42					
	(b) Merchandise bought for sale			51 935 06					
	(c) Cost of manufacturing or producing goods (From Schedule A): Salaries and Wages, $ ____ ; Other costs, $ ____ ; Total								
	(d) Total of Items (a), (b), and (c)			90 442 48					
	(e) Less Inventory at end of year			20 942 18			69 500 30		
3.	Gross Profit from Trading or Manufacturing (Item 1 minus Item 2)							5 151 26	
4.	Gross Profit from Operations Other Than Trading or Manufacturing. (Give nature of business):								
	(a)								
	(b)								
	(c)								
5.	Interest on Bank Deposits, Notes, Mortgages, and Corporation Bonds							27 736 16	
6.	Rents							876 70	
7.	Royalties								
8.	Profit from Sale of Real Estate, Stocks, Bonds, and other Capital Assets (From Schedule D)							2 970 08	
9.	Dividends on Stock of Domestic Corporations							10 446 00	
10.	Other Income (including dividends received on Stock of foreign corporations). (Give nature of income):								
	(a)								
	(b)								
	(c)								
11.	Total Income (or Items 3 to 10)								$ 39 07819
	DEDUCTIONS								
12.	Compensation of Officers (From Schedule C)							None	
13.	Rent on Business Property							2 040 00	
14.	Repairs (From Schedule E); Salaries and Wages, $ ____ ; Other Costs, $ ____ ; Total								
15.	Interest								
16.	Taxes (From Schedule H)							1 229 55	
17.	Losses (From Schedule F) Steamship Operations							5 040 40	
18.	Bad Debts (From Schedule G)								
19.	Dividends (From Schedule K)							18 446 08	
20.	Depreciation (resulting from exhaustion, wear and tear, or obsolescence) (From Schedule L)							11 160 00	
21.	Depletion of Mines, Oil and Gas Wells, Timber, etc. (Submit schedule, see Instruction 21)								
22.	Other Deductions Not Reported Above. (Explain below, or on separate sheet): Miscellaneous							4 321 32	
	(a) Salaries and wages. (Not included in Item 3, 13, or 14 above)							8 955 87	
	(b) Net Loss for 1930–1929 (Submit schedule)								
	(c)								
	(d)								
	(e)								
23.	Total Deductions (or Items 12 to 22)								$ 48 29119
24.	Net Income (Item 11 minus Item 23)								$ 6 30500

COMPUTATION OF TAX

25.	Net Income (Item 24 above)	$					26.	Income Tax (12% of Item 27)	$		
25a.	Less Credit of $2,000 (for a domestic corporation having a net income of less than $50,000)						26a.	If net income of domestic corporation is less than $50,000, enter the amount over $50,000			
27.	Balance (Item 25 minus Item 26)	$					28.	Total Tax (Item 26 plus Item 26a)	$		
29.	Less: Income Tax Paid at Source. (This credit can only be allowed to a consolidated foreign corporation)	$									
30.	Income Tax Paid to a Foreign Country or U. S. possession by a domestic corporation (see Inst. 27)										
31.	Balance of Tax (Item 28 minus Items 29 and 30)								$		

An amended return must be marked "Amended" at top of return. Checks and drafts will be accepted only if payable at par

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Page 2 of Return — SCHEDULE E—BALANCE SHEETS (See Instruction 6)

Items	Beginning of Taxable Year — Amount	Beginning of Taxable Year — Total	End of Taxable Year — Amount	End of Taxable Year — Total
ASSETS				
1. Cash		$ 86 595 84		$ 1 642 298 84
2. Notes receivable				
3. Accounts receivable	$ 209 623 99		$ 108 144 88	
Less reserve for bad debts		209 623 99		108 144 88
4. Inventories:				
Raw materials	$		$	
Work in process				
Finished goods	58 589 48		80 942 18	
Supplies				
		58 589 48		80 942 18
5. Investments (nontaxable):				
Obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia	$		$	
Bonds issued under the Federal Farm Loan Act, or under such Act as amended				
Obligations of the United States or its possessions				
6. Other investments:				
Stocks of domestic corporations	$ 804 595 00		$ 764 679	
Bonds of domestic corporations	11 975 00		18 975	
Stocks and bonds of foreign corporations				
All other investments or loans	140 000 00	884 970 00	183 280	710 934
7. Deferred charges:				
Prepaid insurance	$		$	
Prepaid taxes				
All other				
8. Capital assets:				
Land		80 000		80 000
Buildings	$ 80 000		$ 80 000	
Machinery and equipment	7 780 80		7 780 80	
Furniture and fixtures	8 000		8 000	
Delivery equipment				
	$ 95 780 80		$ 95 780 80	
Less reserve for depreciation	4 480 80	88 800 00	4 880 80	88 900
9. Patents				
10. Good will				
11. Other assets (describe fully):				
	$		$	
12. Total Assets		$ 1 010 636 99		$ 2 722 871 76
LIABILITIES				
13. Notes payable (less than one year)		$ 800 000		$ 800 000
14. Accounts payable		4 365 48		19 489 13
15. Bonds and notes (not secured by mortgage)				
16. Mortgages (including bonds and notes so secured)				
17. Accrued expenses:				
Interest	$		$	
Taxes				
All other				
18. Other liabilities (describe fully):				
19. Capital stock:				
Preferred stock (less stock in treasury)	$		$	
Common stock (less stock in treasury)		800 000		2 000 000
20. Surplus	$		$	
21. Undivided profits		6 483 56		18 782 64
22. Total Liabilities		$ 1 010 636 99		$ 2 722 871 76

Remarks

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SCHEDULE L—RECONCILIATION OF NET INCOME AND ANALYSIS OF CHANGES IN SURPLUS

1. Net income from line 31, page 1 of the return			6	306	00	11. Deductible deductions				
2. Deductible income						(a) Donations, gratuities, and contributions				
(a) Interest on obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia						(b) Income and profits taxes paid to the United States, and to each of such taxes paid or to be paid to a possession or foreign country to be claimed as a credit in item 12, page 1 of the return				
(b) Interest on securities issued under the Federal Farm Loan Act, or under such Act as amended						(c) Federal taxes paid on tax-free covenant bonds				
(c) Interest on obligations of the United States or its possessions						(d) Special improvement taxes tending to increase the value of the property assessed				
(d) Dividends deductible under Section 26(g) of the Revenue Act of 1921			18	648	00	(e) Purchases and leases, additions, or betterments treated as expenses on the books				
(e) Proceeds of life insurance policies paid upon the death of the insured						(f) Depreciation not reserved				
(f) Other items of nontaxable income (to be detailed):						(g) Income premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary				
(g)						(h) Interest on indebtedness incurred or continued to purchase or carry obligations or securities the interest upon which is wholly exempt from taxation				
(h)						(i) Additions to reserves for bad debts which are not included in item 10, page 1 of return				
(i)						(j) Additions to reserves for contingencies, etc. (to be detailed):				
3. Changes against reserves for bad debts, if item 10, page 1 of return is not on addition to a reserve						(k)				
4. Changes against reserves for contingencies, etc. (to be detailed):						(l)				
(j)						(m)				
(k)						(k) Other nondeductible deductions (to be detailed):				
(l)						(l)				
5. Total of Lines 1 to 4, inclusive			6	324	00	(m)				
6. Total from Line 31						12. Total of Lines 11				
7. Net profit for year, as shown by books, before any adjustments made thereto (Line 5 minus Line 6)						13. Dividends paid during the taxable year (state whether paid in cash, stock of the corporation, or other property):				
8. Surplus and undivided profits as shown by balance sheet at close of preceding taxable year			6	451	84	(a) Date paid _____ Character _____				
9. Other credits to surplus (to be detailed):						(b) Date paid _____ Character _____				
(a)						(c) Date paid _____ Character _____				
(b)						(d) Date paid _____ Character _____				
(c)						14. Other debits to surplus (to be detailed):				
10. Total of Lines 7 to 9, inclusive						(a)				
11. Total from Line 31						(b)				
12. Surplus and undivided profits shown by balance sheet at close of taxable year (Line 10 minus Line 11)			12	775	84	(c)				
						15. Total of Lines 12 and 14				

QUESTIONS

KIND OF BUSINESS

1. By means of the key letters given below, identify the corporation's main income-producing activity with one of the general classes, and follow this by a special classification of the business sufficient to give the information called for under each general class.

A—Agriculture and related industries, including fishing, logging, tea harvesting, etc., and also the leasing of such property. State the product or products. B—Mining and quarrying, including gas and oil wells, and also the leasing of such property. State the product or products. C—Manufacturing. State the product and also the material if not implied by the name of the product. D—Construction—general contractors, buildings, bridges, railroads, ships, etc., also equipping and installing same with appliances, devices, or machinery, without their manufacture. State nature of structures built, contracts taken, or kind of installations. E—Transportation—rail, water, local, etc. State the kind of special product transported, if any. F—Public utilities—gas (natural, coal, or water); electric light or power (hydro or steam generated); heating (steam or hot water); telephone; waterworks or power. G—Storage—without trading or profit from sales—(elevators, warehouses, stockyards, etc.). State product stored. H—Leasing (transportation or utilities. State kind of property. I—Trading in goods bought and not produced by the trading concern. State manner of trade, whether wholesale, retail, or commission, and product handled. Also with storage with profit primarily from sales. J—Service—domestic, including hotels, restaurants, etc.; amusements; other professional, personal, or industrial service. State the service. K—Finance, including banking, real estate, insurance. L—Concerns not falling in above classes (a) because of combining several of them with no predominant business, or (b) for other reasons.

2. Concerns whose business involves activity falling in two or more of the above general classes, where the same product is concerned, should report business so identified with but one of the above general classes; for example, concerns in A or B which also transport and market their own product exclusively or mainly, should still be identified with classes A or B; concerns in C (manufacturing) which own or control their source of material supply in A or B and which also transport, sell, or install their own product exclusively or mainly, should be identified with manufacturing; concerns in D may control or own the source of supply of materials used exclusively or mainly in their constructive work; concerns in E or H may own or control the source of their material or power; concerns in F may transport or store their own merchandise, but its production would identify them with A, B, or C.

3. Answer:

(a) General class (use key letter designation) _____

(b) State income-producing business (give specifically the information called for under each key letter, also whether acting as principal, or as agent on commission; state if inactive or in liquidation)

AFFILIATIONS WITH OTHER CORPORATIONS

SEE INSTRUCTION 10

4. Is this a consolidated return of two or more corporations? No

If so, procure from the Collector of Internal Revenue for your district Form 851, Affiliations Schedule, which shall be filed in, sworn to, and filed as a part of this return. See Article 13 (d) and (e), Regulations 74.

5. Did the corporation file a consolidated return for the preceding taxable year? _____

PREDECESSOR BUSINESS

6. Did the corporation file a return under the same name for the preceding taxable year? Yes Was the corporation in any way an outgrowth, result, continuation, or reorganization of a business or businesses in existence during this or any prior year since December 31, 1917? _____ If answer is "yes," give name and address of each predecessor business, and the date of the change in entity. _____

Upon such change were any asset values increased or decreased? _____ If the answer is "yes," closing balance sheets of old business and opening balance sheets of new business must be furnished.

BASIS OF RETURN

7. Is this return made on the basis of actual receipts and disbursements? Yes If not, describe fully what other basis or method was used in computing net income. _____

VALUATION OF INVENTORIES

8. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower. If other basis was used, describe fully, state why used and the date inventory was last reconciled with cash. _____

Cost

LIST OF ATTACHED SCHEDULES

9. Enter below a list of all schedules accompanying this return, giving for each a brief title and the schedule number. The name and address of the corporation should be placed on each separate schedule accompanying the return.

The corporation's books are in care of _____

Located at 1512 Russ Building, San Francisco.

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In the United States Circuit Court of Appeals
for the Ninth Circuit

B. T. A. Docket No. 83397

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.), a corporation,
Petitioner on Review,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

B. T. A. Docket No. 93668

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.), a corporation,
Petitioner on Review,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

ORDER FOR CONSOLIDATION OF THE RECORD

Upon consideration of the motion filed herein by counsel for the petitioner on review in the above-entitled proceedings, moving the Court to consolidate said proceedings for purposes of record, briefing, hearing and decision, and for other purposes, it is this 10th day of March, 1941.

Ordered that the said motion be and it is hereby granted.

And It Is Further Ordered that a certified copy of [168] the motion and this order be transmitted by the Clerk of this Court to the Clerk of the United States Board of Tax Appeals.

(s) CURTIS D. WILBUR
U. S. Circuit Judge.

A true copy.

Attest: March 10, 1941.

[Seal] PAUL P. O'BRIEN,
Clerk.

By FRANK A. SCHMID,
Deputy Clerk.

[Endorsed]: Filed March 10, 1941. Paul P. O'Brien, Clerk.

[Endorsed]: U. S. B. T. A. Filed March 14, 1941. [169]

[Title of Board and Cause.]

DESIGNATION OF CONTENTS OF RECORD ON APPEAL

In compliance with the provisions of paragraph (a) of Rule 75 of the Rules of Civil Procedure for the District Courts of the United States as made applicable to review of a decision of the United States Board of Tax Appeals by Rule 30 of the Rules of the United States Circuit Court of Ap-

peals for the Ninth Circuit, the above-named petitioner hereby designates the portions of the record, proceedings, and evidence to be contained in the record on review of the above-entitled proceedings, as follows:

1. Docket entries of the proceedings before the Board of Tax Appeals.
2. Motion for order and order granting leave to file amended petition.
3. Amended petition filed July 10, 1939.
4. Answer to amended petition filed July 31, 1939.
5. Stipulation of facts filed in the proceeding, excepting there- [170] from copies of bills of sale of enrolled vessels attached thereto and referred to as Exhibits A and B to said stipulation.
6. Finding of Fact and Memorandum Opinion of the Board promulgated May 22, 1940.
7. Decision of the Board of Tax Appeals entered August 6, 1940.
8. Petition for Review of Decision of the Board by the United States Circuit Court of Appeals for the Ninth Circuit, filed October 31, 1940.
9. Notice of filing of petition for review and admission of service thereof.
10. Orders enlarging time for preparation, transmission and delivery of the record [not included in record].
11. Revised Statement of the Evidence.
12. Designation of contents of record on appeal.
13. Statement of Points on which petitioner intends to rely.

14. Petitioner's Exhibits 3, 4, 5, 6, 7, 8, 9, 10, 11, 18, 19, 20, 21, 22 and 23 and Respondent's Exhibits A, B and C.

15. Order of the United States Circuit Court of Appeals, Ninth Circuit, for consolidation of the record.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Counsel for Petitioner,
1110 Balfour Building,
San Francisco, California.

Service of the foregoing designation of the contents of the record on appeal is hereby admitted and agreed to this 11th day of March, 1941.

J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent on Review.

[Endorsed]: U. S. B. T. A. Filed March 11, 1941.

[171]

[Title of Board and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 171, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above num-

bered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 20th day of March, 1941.

B. D. GAMBLE,
Clerk, United States Board of Tax Appeals. [172]

[Endorsed]: No. 9781. United States Circuit Court of Appeals for the Ninth Circuit. Wilson Brothers and Company, (Wilson Bros. & Co.,) a corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed March 31, 1941.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 9781 B. T. A.
Docket No. 83397

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.), a corporation,
Petitioner on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

NOTICE OF ADOPTION OF DESIGNATION OF CONTENTS OF RECORD AND STATEMENT OF POINTS FILED WITH THE BOARD OF TAX APPEALS.

To the Honorable Justices of the United States Circuit Court of Appeals for the Ninth Circuit:

Notice is hereby given that the Petitioner on Review in the above entitled proceedings hereby adopts for the purposes of petition on review to the above entitled court, the Designation of Contents of Record and Statement of Points filed with the Clerk of the United States Board of Tax Appeals in the above numbered proceedings on March 11, 1941.

Dated this 16th day of April, 1941.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for the Above
Named Petitioner.

[Endorsed]: Filed April 17, 1941. Paul P. O'Brien, Clerk. [173]

No. 9782

United States

Circuit Court of Appeals

For the Ninth Circuit.

WILSON BROTHERS AND COMPANY, (Wilson Bros. & Co.,) a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Transcript of the Record

Upon Petition to Review a Decision of the United States Board of Tax Appeals.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

APPEARANCES:

For Taxpayer:
A. E. GRAUPNER.

For Comm'r:
T. M. MATHER,
ALVA C. BAIRD.

Docket No. 83397

WILSON BROTHERS AND COMPANY,
(WILSON BROS. AND COMPANY,
a Corporation),

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1936

Mar. 25—Petition received and filed. Taxpayer notified. (Fee paid).

Mar. 25—Copy of petition served on General Counsel.

Apr. 30—Answer filed by General Counsel.

May 5—Copy of answer served on taxpayer.

1937

May 1—Hearing set week of July 6, 1937, San Francisco, Calif.

May 20—Motion for a continuance filed by General Counsel. Granted.

1939

Mar. 25—Hearing set May 29, 1939 in San Francisco, California.

June 6-7—Called 5/29/39. Hearing had before Mr. Disney on merits. Submitted. Motion to consolidated Dockets 83397 and 93668 granted. Stipulation as to the facts filed. Briefs due Aug. 1, 1939, Reply 9/1/39.

June 24—Transcript of hearing of June 6, 1939, filed.

June 24—Transcript of hearing of June 7, 1939, filed.

July 5—Motion for leave to file amended petition filed by taxpayer. Amended petition lodged. 7/10/39 granted. 7/11/39 copy served on General Counsel.

July 28—Brief filed by taxpayer. 8/2/39 copy served on General Counsel.

July 31—Answer to amended petition filed by General Counsel.

Aug. 1—Brief filed by General Counsel.

Aug. 3—Copy of answer to amended petition served on taxpayer.

Aug. 29—Reply brief filed by taxpayer.

1940

May 22—Memorandum opinion rendered, Richard L. Disney, Div. 4. Decision will be entered under Rule 50.

June 17—Motion for review by the entire Board or for reconsideration filed by taxpayer.

June 20—Computation of deficiency filed by General Counsel.

1940

June 28—Order denying petitioner's motion for reconsideration, entered.

July 2—Order denying review by the Board, entered. [1*]

1940

July 9—Hearing set July 31, 1940 on settlement.

July 22—Consent to settlement filed by taxpayer.

Aug. 6—Decision entered, R. L. Disney, Div. 4.

Oct. 31—Petition for review by United States Circuit Court of Appeals, Ninth Circuit, with assignments of error filed by taxpayer.

Oct. 31—Affidavit of service filed by taxpayer.

Nov. 1—Proof of service of petition for review filed.

Dec. 30—Certified copy of an order from 9th Circuit extending time to 2/3/41 to complete and transmit record, filed.

1941

Jan. 8—Statement of evidence filed by taxpayer.

Feb. 3—Certified copy of order from the 9th Circuit enlarging the time to 4/3/41 within which to prepare, transmit and file record, filed.

Mar. 11—Agreed revised statement of evidence filed.

Mar. 11—Statement of points on which petitioner intends to rely filed, with proof of service thereon.

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*Page numbering appearing at foot of page of original certified Transcript of Record.

Mar. 11—Agreed designation of contents of record filed, with proof of service thereon.

Mar. 14—Certified copy of order from the 9th Circuit, consolidating 83397 and 93668, filed.

[2]

United States Board of Tax Appeals
Docket No. 83397

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.), a corporation,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

MOTION FOR ORDER GRANTING LEAVE TO FILE AMENDED PETITION.

Now comes the petitioner above-named by its counsel, Adolphus E. Graupner and Louis D. Janin, and moves this Honorable Board to grant petitioner leave to file an amended petition in the above-entitled proceeding, which said amended petition is presented herewith for consideration on this motion.

The foregoing motion is made in order to have the pleadings accord with the proofs submitted at the hearing of this proceeding in San Francisco,

California, on June 6th and 7th, 1939, and to comply with the provisions of Rule 6(e) of this Board.

Dated, July 1, 1939.

Respectfully submitted,
ADOLPHUS E. GRAUPNER,
LOUIS D. JANIN,
Counsel for Petitioner.

Granted July 10, 1939.

(Signed) R. L. DISNEY,
Member U. S. Board of Tax Appeals.

[Endorsed]: U. S. B. T. A. Filed July 5, 1939.

[3]

[Title of Board and Cause.]

AMENDED PETITION

Upon consent of the above-entitled Board to amend the petition in the above-entitled proceeding to conform to the proofs submitted at the hearing thereof and without waiver of right to challenge the constitutionality of any part of any Revenue Act involved in this proceeding or any act of the Commissioner of Internal Revenue or his subordinate, or to object to the jurisdiction of this Board, the above named petitioner hereby petitions for a redetermination of the alleged deficiency set forth by the Commissioner of Internal Revenue in his purported notice of deficiency (IT:E:Aj-RLT-25579-90D) dated December 30, 1935, and as a basis of this proceeding alleges as follows:

1. The petitioner is a corporation duly organized and existing under the laws of the State of Nevada, with its principal office at 1112 Russ Building in the City and County of [4] San Francisco, State of California.

2. The purported notice of deficiency upon which this petition is based (a copy of which is hereunto attached and marked Exhibit "A") was apparently mailed to the petitioner on December 30, 1935.

3. The asserted deficiency in tax here in controversy is for alleged income taxes for the calendar years 1932 and 1933 and, as asserted in said purported deficiency notice, in the amount of not more than $11,343.36 for the year 1932 and in the amount of not more than $22,078.01 for the year 1933, or for not more than the sum of $33,421.37 for the said two years.

4. The alleged determination or proposal of a deficiency in tax set forth in said purported notice of deficiency is erroneous in each and every of the following particulars assigned as errors:

(a) The Commissioner erred in proposing, determining and asserting against petitioner any amount as a deficiency in income tax for either of the calendar taxable years 1932 and 1933.

(b) The Commissioner erred in holding that petitioner was availed of for the purpose of preventing the imposition of surtax or any internal revenue tax upon its shareholders for either or both of the taxable years herein involved, or that petitioner is liable for any additional tax or tax penalty for per-

mitting its gains and profits to accumulate instead of being divided or distributed to its shareholders, or that it in anyway violated, or is subject to taxation or penalty under, the provisions of section 104 of the Revenue Act of 1932 for the years [5] 1932 and 1933.

(c) The Commissioner erred in disallowing the amount of $5,225.02 as depreciation claimed by petitioner as a deduction for the taxable calendar year 1932, and in not allowing at least $2,326.08 depreciation in addition to that claimed on the return for said year.

(d) The Commissioner erred in disallowing the amount of $13,975.02 as depreciation claimed by petitioner as a deduction for the taxable calendar year 1933.

(e) The Commissioner erred in disallowing the amount of $4,547.05 claimed by petitioner as a deductible loss on steamship operation for the taxable year 1932.

(f) The Commissioner erred in disallowing the amount of $4,412.26 claimed by petitioner as a deductible loss on steamship operation for the taxable year 1933.

(g) The Commissioner erred in failing to determine the proper adjusted basis for depreciation as of December 31, 1931, on the steamships "Idaho" and "Oregon" and on the furniture and fixtures belonging to petitioner and in using an erroneous alleged "cost" as such basis.

(h) The Commissioner erred in adding to petitioner's income, as returned by it for the taxable year 1932, the amount of $5,442.32 as taxable income received by way of interest from bank deposits.

(i) The Commissioner erred in adding to petitioner's income, as returned by it for the taxable year 1933, the amount of $445.18 as taxable income received by way of interest from [6] bank deposits.

(j) The Commissioner erred in adding to petitioner's income, as returned by it for the taxable year 1933, the amount of $2,160.80 by disallowance thereof as deduction for bad debts.

(k) The Commissioner erred in adding to petitioner's income, as returned by it for the taxable year 1932, the amount of $18,258.00 representing dividends received by it from domestic corporations subject to tax.

(l) The Commissioner erred in adding to petitioner's income, as returned by it for the taxable year 1933, the amount of $17,541.00 representing dividends received by it from domestic corporations subject to tax.

(m) The Commissioner erred in adding to the tax returned by petitioner for the taxable year 1932 and the erroneous and illegal computation of an alleged deficiency made by him of the amount of $567.17 as a penalty pretended to be imposed for negligence as defined by section 293(a) of the Revenue Act of 1932.

(n) The Commissioner erred in adding to the

tax returned by petitioner for the taxable year 1933 and the erroneous and illegal computation of an alleged deficiency made by him of the amount of $1,-103.90 as a penalty pretended to be imposed for negligence as defined by section 293(a) of the Revenue Act of 1932.

(o) The Commissioner erred in attempting to compute any deficiency in income tax against petitioner for either or both of the taxable years 1932 and/or 1933, and particularly in attempting to compute any deficiency in income tax against petitioner [7] for either or both of said years under the provisions of section 104 of the Revenue Act of 1932.

5. The facts upon which petitioner relies as a basis for this proceeding are as follows:

(a) Petitioner is a corporation duly organized on December 14, 1928, under the laws of the State of Nevada. Its correct name and title is "Wilson Bros. & Co." instead of "Wilson Brothers and Company" as stated in the Notice of deficiency. Its sole stockholders are Francis A. Wilson and Winfred T. Wilson.

(b) Petitioner was formed to take over the business of a copartnership of the same name and to acquire, own and operate timberlands, saw mills, logging railroads and equipment, and steamships; also, to buy, sell and transport lumber, to own, operate and maintain steamships and to utilize the same for the transport of cargoes.

(c) During said taxable years petitioner kept and maintained its books of account on the accrual basis.

(d) On or about March 31, 1933, petitioner filed its income tax return for the taxable year 1932 in which it reported no taxable income for said year. Said return stated specifically the items of petitioner's gross income, the deductions and credits claimed by it.

(e) On or about March 15, 1934, petitioner filed its income tax return for the taxable year 1933 in which it reported no taxable income for said year. Said return stated specifically the items of petitioner's gross income, the deductions and credits claimed by it. [8]

(f) The Commissioner has erroneously and illegally proposed and determined a deficiency in income tax against petitioner for the taxable year 1932 in the amount of $477.61, an additional tax for said year in the amount of $10,865.75 by erroneously and illegally applying the terms of section 104(a) to the income of petitioner, and a penalty of five percentum on the sum of the above mentioned amounts by illegally applying section 293(a) of the Revenue Act of 1932 to the return filed by petitioner as aforesaid, or a total of deficiency and penalty of $11,910.53.

(g) The Commissioner has erroneously and illegally proposed and determined a deficiency in income tax against petitioner for the taxable year 1933 in the amount of $2,870.25, an additional tax for said year in the amount of $19,207.76 by erroneously applying the terms of section 104(a) to the

income of petitioner, and a penalty of five percentum on the sum of the above mentioned amounts by illegally applying section 292(a) of the Revenue Act of 1932 to the return filed by petitioner as aforesaid, or a total deficiency and penalty of $23,-181.91.

(h) Respondent added to the amount of total income reported by petitioner in its income tax returns for the respective years 1932 and 1933, under designation in the deficiency notice for said years as "Excessive depreciation", the following amounts:

For the year 1932 ..... $ 5,225.02,
For the year 1933 ..... 13,975.02

Petitioner has claimed as deductible depreciation in its return for said years the following and only the following items and amounts with respect to assets used in the trade or business, viz: [9]

Depreciable Items	1932	1933
Wooden Buildings	$ 1,000.00	$ 1,000.00
Steamships "Idaho" and "Oregon"	8,750.00	17,500.00
Furniture and Fixtures	500.00	500.00
Automobiles	900.00	1,649.85
Or a total of	$11,150.00	$20,649.85

Respondents disallowance of items of deduction in the deficiency notice in this proceeding has not been itemized or specifically explained therein or in his answer to the original petition on file herein or by proofs at hearing of this proceeding.

(i) Petitioner has stipulated to the disallowance of depreciation claimed on wooden buildings in the

total amount claimed for each of the years 1932 and 1933. Petitioner has also stipulated that the allowable depreciation on automobiles for each of the two years involved is $900.00 for the year 1932 and $1,649.85 for the year 1933.

(j) The basis to petitioner for depreciation of its 75% interest in the steamship "Idaho", without allowance for depreciation in prior years, was on December 31, 1931, at least $200,216.67; the depreciation claimed and allowed by respondent to said date was $108,750.00, as has been stipulated; the petitioner's depreciable basis on said steamship as adjusted for depreciation allowed and allowable for years prior to December 31, 1931, was at least $91,466.67.

(k) As determined in said deficiency notice said steamship "Idaho" had a useful depreciable life of not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date; and petitioner [10] is and was entitled to an annual depreciation allowance of not less than $6,097.11 for said period.

(l) The basis to petitioner for depreciation on its 100% interest in the steamship "Oregon", without allowance for depreciation in prior years, was on December 31, 1931, at least $205,766.32; the depreciation claimed and allowed by respondent to said date was $109,231.69, as has been stipulated; the petitioner's depreciable basis on said steamship as of December 31, 1931, as adjusted for depreciation al-

lowed and allowable for prior years was at least $96,434.63.

(m) As determined in said deficiency notice said steamship "Oregon" had a useful depreciable life not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date, and petitioner is and was entitled to an annual depreciation allowance of not less than $6,437.64 for said period.

(n) On January 2, 1929, petitioner acquired furniture and fixtures of a fair market value of $5,000.00, on which respondent has determined a useful depreciable life of ten years from December 31, 1931. Respondent has allowed $1,500.00 depreciation on said furniture and fixtures to December 31, 1931, and determined a rate of depreciation of 10% on the remaining ten years of life thereof. Petitioner is therefore entitled to allowance for depreciation on said furniture and fixtures in an amount not less than $350.00 per annum for each of the taxable years 1932 and 1933.

(o) During the taxable years 1932 and 1933 petitioner was required to protect, maintain and keep in repair the steam- [11] ships "Idaho" and "Oregon" in order to keep such vessels in seaworthy condition and prevent their undue deterioration and depreciation. For such purpose petitioner expended the amount of $4,547.05 during the taxable year 1932 and the amount of $4,412.26 during the taxable year 1933. Such expenditures were proper and necessary business expenses and petitioner is entitled to de-

duct said amounts for the respective years despite the disallowance of the same by the respondent.

(p) During the years 1932 and 1933 and prior thereto, petitioner was the managing agent for the steamship "Svea" and as such was required to protect, maintain and keep said vessel in repair. Petitioner was not an owner of any interest in said steamship but as agent was required to perform the services mentioned. Due to said steamship being laid up and making no earnings from which petitioner might reimburse itself and the refusal of the owners to contribute to such expense, petitioner in the year 1933 wrote-off the amount of $2,160.80 as a partial write-off of a bad debt. Said write-off was made after attempts to collect the same from the shareowners of said steamship and advice of counsel that petitioner had no right of recovery and the determination by petitioner that said amount was beyond hope of recovery.

(q) Petitioner is therefore entitled to deduct from its gross income for the years 1932 and 1933 as reported in its income tax returns for the respective years the following statutory deductible items: [12]

Deductions	1932	1933
Rent, as accepted by respondent	$ 1,415.50	$ 1,140.00
Taxes, as accepted by respondent	752.39	1,284.18
Steamship operations (maintenance)	4,547.05	4,412.26
Dividends, as accepted by respondent	18,258.00	17,541.00
Depreciation—Steamship "Idaho" 75% interest	6,097.77	6,097.77
Steamship "Oregon" 100% interest	6,437.64	6,437.64
Automobiles, as accepted	900.00	1,649.85
Furniture and fixtures	350.00	350.00
Bad debts, as accepted by respondent		19,223.24
Deduction for partial write-off of advancements steamship "Svea"		2,160.80
Salaries and wages, as accepted by respondent	5,780.00	5,785.00
General expense, as accepted by respondent	2,403.52	3,501.70
	$46,941.67	$69,583.44

(r) During the years 1932 and 1933 petitioner in its income tax returns reported for said years respectively the amounts of $12,949.58 and $9,035.81 as income from interest. Respondent without explanation in his deficiency notice or affirmative pleading in his answer in this proceeding asserted interest on bank deposits to be taxable in the amount of $5,442.32 for the year 1932 and $445.18 for the year 1933 and in his deficiency notice added said amounts to petitioner's income for the said respective years, although petitioner had reported as taxable income from interest on bank deposits amounts in excess of said addition, and although no

amounts of interest in addition to [13] that reported were paid to or accruable to petitioner for said years or either of them.

(s) Petitioner's gross income was correctly reported in its income tax returns for the years 1932 and 1933 as follows:

	1932	1933
Gross income returned	$ 32,565.57	$75,579.28
From which should be deducted at least	46,941.87	69,583.44
Resulting in net taxable income of	($–14,476.30)	$ 5,995.84

(t) Petitioner was not formed or availed of for the purpose of preventing the imposition of any surtax or internal revenue tax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed.

(u) During the years 1932 and 1933 the economic and financial depression which started in 1929 continued and the impaired and shrunken market value of the assets of petitioner made it inadvisable under sound business practice to declare any dividends or in any other way further impair the assets of the corporation and thus endanger the accomplishment of the business purposes for which petitioner was organized.

(v) Under the facts of this proceeding petitioner is not liable for surtax under section 104 of the Revenue Act of 1932 as amended in any amount upon any possible fair adjustment of its net income

for the taxable calendar years 1932 and 1933. [14]

(w) Under the facts of this proceeding petitioner is not liable for the penalty of five percent sought to be imposed by respondent under the alleged authority of section 293(a) of the Revenue Act of 1932, because the deficiency notice and the testimony adduced shows no negligence, or intentional disregard of rules and regulations, and respondent failed to offer any proof in support of his attempt to impose such a penalty.

Wherefore, the petitioner prays that this Board may hear the proceeding and grant to petitioner such relief from the deficiency, additional tax and penalty asserted by the Commissioner as may be within the jurisdiction of the Board.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for Petitioner,
1110 Balfour Building,
San Francisco, California.

[15]

State of California,
City and County of San Francisco—ss.

Francis A. Wilson, being duly sworn, says that he is the president of the above named incorporated petitioner and that he is authorized to verify the foregoing petition; that he has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true, except as to those facts stated to be upon infor-

mation and belief, and those facts he believes to be true.

FRANCIS A. WILSON

Subscribed and sworn to before me this 30th day of June, 1939.

HAZEL E. THOMPSON

Notary Public in and for the City and County of San Francisco, State of California.

My Commission Expires September 21, 1942. [16]

EXHIBIT "A"

Office of
Commissioner of Internal Revenue
TREASURY DEPARTMENT
Washington

Dec. 30, 1935

Wilson Brothers and Company,
1112 Russ Building,
San Francisco, California.

Sirs:

You are advised that the determination of your income tax liability for the years 1932 and 1933, discloses a deficiency of $35,092.44, tax and penalty as shown in the statement attached.

In accordance with section 272(a) of the Revenue Act of 1932, as amended by section 501 of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a

redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue Washington, D. C., for the attention of IT:C:P-7. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner.

By W. T. SHERWOOD
Acting Deputy Commissioner.

Enclosures:
Statement
Form 870
Schedule A [17]

STATEMENT

In re: Wilson Brothers and Company,
1112 Russ Building,
San Francisco, California.

Year	Tax Liability	Tax Assessed	Deficiency	5% Penalty
(Consent on 1932 to 12/30/35)				
1932	$11,343.36	None	$11,343.36	$ 567.17
1933	22,078.01	None	22,078.01	1,103.90
Totals	$33,421.37	None	$33,421.37	$1,671.07
Total deficiencies and penalties				$35,092.44

The report of the internal revenue agent in charge at San Francisco, California has been reviewed and is approved by this office.

After careful consideration of your Federal income tax returns and of all other available information the Bureau holds that your corporation is subject to taxation under the provisions of section 104 of the Revenue Act of 1932 for the years 1932 and 1933.

1932

Net loss reported on return		$11,740.89
Add:		
1. Excessive depreciation	$5,225.02	
2. Loss on steamship operation	4,547.05	
3. Interest	5,442.32	15,214.39
Net income adjusted, section 21		$ 3,473.50
Add:		
Dividends received		18,258.00
Net income adjusted, section 104(c)		$21,731.50

[18]

EXPLANATION OF ADJUSTMENTS

1. The excessive depreciation has been disallowed in accordance with section 23(k) of the Revenue Act of 1932 and Treasury Decision 4422. The computation of the depreciation allowable is shown in schedule A attached.

2. The loss on steamship operation has been disallowed for the reason no evidence has been submitted to substantiate the loss as a deduction allowable under the provisions of section 23 of the Revenue Act of 1932.

3. Interest on bank deposits constitutes taxable income in accordance with section 22 of the Revenue Act of 1932.

COMPUTATION OF TAX

Net income, section 21	$ 3,473.50	
Tax liability at 13 3/4%, section 13(a)		$ 477.61
Net income, section 104(c)	21,731.50	
Tax liability at 50%, section 104(a)		10,865.75
Total tax liability		$11,343.36
Tax assessed		None
Deficiency		$11,343.36
5% penalty		567.17
Total deficiency and penalty		$11,910.53

1933

Net loss reported on return		$ 118.75
Add:		
1. Excessive depreciation	13,975.02	
2. Reserve for bad debts	2,160.80	
3. Loss on steamship operation	4,412.26	
4. Interest	445.18	20,993.26
Net income adjusted, section 21		$20,874.51

[19]

Brought forward	$20,874.51
Add:	
Dividends	17,541.00
Net income adjusted, section 104(c)	$38,415.51

EXPLANATION OF ADJUSTMENTS

1. See #1 under 1932.

2. The reserve for bad debts has been disallowed in accordance with section 23(j) of the Revenue Act of 1932, since your basis as established

is the actual bad debt basis and no permission has been granted by the Commissioner to change to the reserve basis.

3. See #2 under 1932.
4. See #3 under 1932.

COMPUTATION OF TAX

Net income, section 21	$20,874.51	
Tax liability at 13¾%, section 13(a)		$ 2,870.25
Net income, sections 104(c)	38,415.51	
Tax liability at 50%, section 104(a)		19,207.76
Total tax liability		$22,078.01
Tax assessed		None
Deficiency		$22,078.01
5% penalty		1,103.90
Total deficiency and penalty		$23,181.91

[20]

The understatement of tax for the years 1932 and 1933 is attributable to negligence as defined in the regulations and under the provisions of section 293(a) of the Revenue Act of 1932 and a penalty of 5% of each deficiency attaches. The 5% penalty is included in the above assessments.

The interest due on the deficiencies in accordance with the provisions of section 292 of the Revenue Act of 1932 will be computed by this office and demanded by the collector of internal revenue at the time you are called upon to pay the tax.

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him. [21]

Kind of Property	Date Built	Cost	Interest Owned by Wilsons	Interest	Depreciation Deducted to Dec. 31, 1928	Date Acquired by Taxpayer	Cost	Depreciation Deducted to Dec. 31, 1931	Residual Cost Jan. 1, 1932	Rate From Jan. 1, 1932	Depreciation 1932	Allowable 1933
S. S. Idaho	1916	$200,000.00	75%	$150,000.00	$90,000.00	January 2, 1929	$60,000.00	$18,750.00	$41,250.00	6⅔%	$2,750.00	$2,750.00
S. S. Oregon	1916	140,386.15	100%	140,386.15	84,231.69	January 2, 1929	56,154.48	25,000.00	31,154.46	6⅔%	2,076.96	2,076.96
Wooden building	1916	7,500.00			4,875.00	January 2, 1929	2,625.00	3,000.00	None		None	None
Furniture and fixtures						January 3, 1929	3,480.20	1,500.00	1,980.20	10 %	198.02	198.02
Automobiles						1932			8,249.25	5 %	900.00	1,649.85
Total											$5,924.98	$6,674.83

[Endorsed]: U.S.B.T.A. Lodged July 5, 1939. Filed July 10, 1939.

[22]

[Title of Board and Cause.]

ANSWER TO AMENDED PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the amended petition filed by the above-named petitioner, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the amended petition.

2. Admits the allegations of fact contained in paragraph 2 of the amended petition.

3. Admits that the deficiency in tax here in controversy is for taxes for the calendar years 1932 and 1933 as asserted in the deficiency notice, as alleged in paragraph 3 of the amended petition, but denies the remaining allegations contained in said paragraph. [23]

4. (a) to (c), inclusive. Denies the Commissioner erred in the determination of the deficiency as alleged in subparagraphs (a) to (c), inclusive, of paragraph 4 of the amended petition.

5. (a) Admits the allegations contained in subparagraph (a) of paragraph 5 of the amended petition.

(b) Denies the allegations contained in subparagraph (b) of paragraph 5 of the amended petition.

(c) Admits the allegations contained in sub-

paragraph (c) of paragraph 5 of the amended petition.

(d) Admits on or about March 31, 1933, petitioner filed its income tax return for the taxable year 1932 in which it reported no taxable income for said year as alleged in subparagraph (d) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(e) Admits on or about March 15, 1934, petitioner filed its income tax return for the taxable year 1933 in which it reported no taxable income for said year, as alleged in subparagraph (e) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(f) Denies the allegations contained in subparagraph (f) of paragraph 5 of the amended petition.

(g) Denies the allegations contained in subparagraph (g) of paragraph 5 of the amended petition.

(h) Admits respondent added to the amount of income reported by the petitioner for the year 1932 $5,225.02 and for the year 1933 [24] $13,975.02 as excessive depreciation, as alleged in subparagraph (h) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(i) Admits the allegations contained in sub-

paragraph (i) of paragraph 5 of the amended petition.

(j) Admits the depreciation allowed by respondent was $108,750.00 as stipulated, as alleged in subparagraph (j) of Paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(k) Admits, as determined in said deficiency notice said steamship "Idaho" had a useful depreciable life of not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date, as alleged in subparagraph (k) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(l) Admits the depreciation allowed by respondent was $109,231.69 as stipulated, as alleged in subparagraph (l) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(m) Admits, as determined in said deficiency notice said steamship "Oregon" had a useful depreciable life not in excess of fifteen years from January 1, 1932, and an annual rate of depreciation of 6⅔ per cent from said date, as alleged in subparagraph (m) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph. [25]

(n) Denies the allegations contained in subparagraph (n) of paragraph 5 of the amended petition.

(o) Denies the allegations contained in sub-

paragraph (o) of paragraph 5 of the amended petition.

(p) Denies the allegations contained in subparagraph (p) of paragraph 5 of the amended petition.

(q) Denies the allegations contained in subparagraph (q) of paragraph 5 of the amended petition.

(r) Admits during the years 1932 and 1933 petitioner in its income tax returns reported for said years respectively the amounts of $12,949.58 and $9,035.81 as income from interest, as alleged in subparagraph (r) of paragraph 5 of the amended petition, but denies the remaining allegations contained in said subparagraph.

(s) Denies the allegations contained in subparagraph (s) of paragraph 5 of the amended petition.

(t) Denies the allegations contained in subparagraph (t) of paragraph 5 of the amended petition.

(u) Denies the allegations contained in subparagraph (u) of paragraph 5 of the amended petition.

(v) Denies the allegations contained in subparagraph (v) of paragraph 5 of the amended petition.

(w) Denies the allegations contained in subparagraph (w) of paragraph 5 of the amended petition. [26]

6. Denies generally and specifically each and every allegation in the amended petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and that the petitioner's appeal be denied.

[Signed] J. P. WENCHEL
TMM
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:
ALVA C. BAIRD.
T. M. MATHER
Special Attorneys,
Bureau of Internal Revenue.

TMM:emb 7-22-39

[Endorsed]: U.S.B.T.A. Filed July 31, 1939. [27]

United States Board of Tax Appeals
Washington

Docket No. 83397.

WILSON BROTHERS & CO.,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION.

Pursuant to the Memorandum Opinion of the Board entered May 22, 1940, the respondent herein having on June 20, 1940, filed a recomputation of

the tax, and the petitioner having on July 22, 1940, filed an acquiescence in said recomputation, now, therefore, it is

Ordered and Decided: That there are deficiencies in normal taxes, surtaxes, and penalties as follows:

Year	Normal Tax	Additional Tax under section 104, 1932 Act	Penalty
1932	None	$ 3,316.84	$165.84
1933	$1,499.93	14,224.80	786.24

Enter:

[Seal] (Signed) R. L. DISNEY
Member. [28]

Entered Aug. 6, 1940.

[Title of Board and Cause.]

PETITION FOR REVIEW OF DECISION OF THE UNITED STATES BOARD OF TAX APPEALS BY THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

To the Honorable, The Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Wilson Brothers and Company (properly entitled Wilson Bros. & Co.), your petitioner, pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code respectfully petitions this Honorable Court to review the decision of the United States Board of Tax Appeals entered on the 6th day of August, 1940, and finding deficiencies in income tax, together with additional

tax under Section 104 of the Revenue Act of 1932 and a negligence penalty under Section 293(a) of said Act in the total of $3,482.68 for the taxable calendar year 1932 and in the total of $16,510.97 for the taxable calendar year 1933. [29]

I

Jurisdiction

Your petitioner is a corporation organized under the laws of the State of Nevada, having, during the taxable years involved, its principal office and place of business in the City and County of San Francisco, State of California. Petitioner timely filed its Federal income tax returns in respect to which the aforementioned tax liabilities arose with the Collector of Internal Revenue, 1st District of California, located in the City and County of San Francisco, State of California, which is situated within the jurisdiction of the United States Circuit Court of Appeals for the Ninth Judicial Circuit.

II

Prior Proceedings

The Commissioner of Internal Revenue, by his letter dated December 30, 1935, asserted a deficiency in petitioner's tax liability for the year 1932 in the sum of $11, 343.36 and a penalty of five percentum in the amount of $567.17, he also asserted a deficiency in petitioner's tax liability for the year 1933 in the sum of $22,078.01 and a penalty of five per centum in the amount of $1,103.90. By his letter of March 8, 1938, the Commissioner asserted a

deficiency in petitioner's tax liability for the year 1934 in the sum of $13,632.27 and a penalty of five percentum in the amount of $681.61.

Thereafter, and within the times prescribed by law, the petitioner filed with the United States Board of Tax Appeals its petitions under the aforesaid two letters requesting the redetermination of such deficiencies. The proceedings duly came on for hearing on June 6, 1939, at which time the two proceedings were [30] consolidated for hearing. The proceedings were submitted to the Board upon a written stipulation of facts, oral testimony of witnesses and documentary evidence applicable to the two proceedings.

Thereafter, and on May 22, 1940, the United States Board of Tax Appeals made its report and rendered a memorandum opinion, through a single member sitting as Division No. 4 of said Board, approving in part the determinations of the Commissioner.

Thereafter, and on August 6, 1940, decisions were made and entered in each of the two proceedings by the United States Board of Tax Appeals whereby final orders of redetermination of deficiencies for the respective years involved were made and entered as follows:

Year	Normal Tax	Additional Tax Under Section 104, 1932 Act and Section 102 1934 Act	Penalty
1932	None	$ 3,316.84	$165.84
1933	$1,499.93	14,224.80	786.24
1934	1,912.05	9,740.70	582.63

III

Statement of the Nature of the Controversy

This proceeding is for the years 1932 and 1933, (Docket No. 83,397) and involves income taxes, together with surtax alleged under the provisions of Section 104 of the Revenue Act of 1932 and a five percentum penalty for asserted negligence under Section 293 (a) of said Act, for the taxable calendar years 1932 and 1933.

The controversy between petitioner (appellant before the Court) and the Commissioner of Internal Revenue involves several issues which, for the years involved, will be presented in the order in which they are discussed in the report or memorandum opinion of [31] the Board of Tax Appeals.

1.(Issue IV (a) in the report or memorandum opinion) Whether the basis for depreciation of petitioner's 75% interest in the steamship "Idaho" adjusted to January 1, 1932 is $52,466.67 as determined in the memorandum opinion, or $91,466.67. This issue is one of law and arises from the difference between the cost ($40,000) of said interest to Henry Wilson and its value $79,000) on February 6, 1917 when he made a gift thereof to his wife, Mary H. Wilson, who in turn made a gift thereof to petitioner on January 2, 1929.

2. (Issue V in the report or memorandum opinion). Whether the petitioner corporation was availed of during the taxable years involved for the purpose of preventing imposition of surtax upon

its two shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed.

3. (Issue VI in the report or memorandum opinion) Whether the petitioner was subject to the five per centum negligence penalty under Section 293(a) of the Revenue Act of 1932.

Due in part to the fact that the report or memorandum opinion of the Board subdivides its findings as it subdivides its opinion on the several issues, thereby disregarding findings of fact made on some issues material to other issues, a consideration of the evidence as well as a consideration of all of the facts found is necessarily involved in the review of the Board's decision.

IV

ASSIGNMENTS OF ERROR

In assigning the errors which petitioner believes to have been committed by the United States Board of Tax Appeals, [32] assignment is made in the order in which the issues were decided and numbered in the report or memorandum opinion of the Board entered May 22, 1940, for the two proceedings docketed and numbered 83,397 and 93,668. For convenience of reference, the issues as considered in the report or memorandum opinion are designated by the Roman numerals, employed in subdividing said report or memorandum opinion into separate parts. No assignments of error are made to issues I and II considered in said report or memorandum opinion.

Petitioner assigns as error the following acts and omissions of said United States Board of Tax Appeals:—

III.

(1) The failure to find and determine that the $43,276.06 account receivable due from the Woodhead Lumber Co. of California was impaired during the year 1934 in at least the amount ($5,000.00) charged off by petitioner in said year against said account as a partial bad debt.

(2) The failure to find and determine that petitioner had fully met its burden of proving error on the part of the respondent in disallowing the claimed deduction of such partial bad debt, such disallowance being predicated entirely on the false assumption that no direct write-off had been made of said $5,000.

(3) The making of a purported finding of fact contrary to the evidence, record and issue involved is as follows:

> "Upon consideration of the entire record we find and determine that the alleged worthless character of the debt from the Woodhead Lumber Co. of California has not been shown. We therefore find and hold that the Commissioner did not err in disallowing the $5,000 deduction claimed." [33]

(4) The failure to find that the cost to petitioner of its bonds of the Kentucky Fuel Gas Corporation were impaired during the year 1934 in at least the amount ($5,500.00) charged off by peti-

tioner in said year against the cost of said bonds as a partial bad debt.

(5) The failure to find and determine that petitioner had fully met its burden of proving error on the part of respondent in disallowing the claimed deduction of such partial bad debt, such disallowance being entirely predicated entirely on the false assumption that no direct write-off had been made of said $5,000.

(6) The making of a purported finding with respect to the deduction of said $5,500 contrary to the evidence, record and issue involved as follows:

> "Obviously such a record does not show error on the part of the Commissioner in denying the deduction."

IV

(7) The failure to allow as a basis for depreciation on the Steamship "Idaho" from January 1, 1932, the amount of $91,377.78 and to determine that petitioner was entitled to deduct depreciation on said steamship for each of the taxable years 1932, 1933 and 1934 in the amount of $6,100.77 per annum.

(8) The failure to allow as a part of the basis of depreciation of the Steamship "Idaho" from January 1, 1932, the amount of $79,000. as the fair market value of a twenty per cent interest therein given to Mary H. Wilson on February 6, 1917, by her husband, at which time said steamship had a fair market value of $395,000., which said twenty

per cent interest was donated to petitioner by said Mary H. Wilson on January 2, 1929. [34]

(9) The determination that the basis (unadjusted) of property acquired by gift prior to December 31, 1920 is changed from the value at the time of said gift to cost to the donor of said gift when said property is made the subject matter of a gift by said donee after December 31, 1920.

V

(10) The making of a purported finding with respect to all of the taxable years involved and without discrimination between the circumstances and facts relating to each of the years 1932, 1933, and 1934, to the effect:

> "We hold that the petitioner was availed of in the taxable years for the purpose of preventing imposition of surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed."

when in fact the record and that part of the record considered in the report or memorandum opinion with respect to such finding is contrary to such finding and said finding is inconsistent with other findings upon which it is purportedly based.

(11) The determination that for the taxable year 1932 petitioner is liable under the alleged authority of Section 104 (a) of the Revenue Act of 1932 in the amount of $3,316.84 as a surtax for the alleged accumulation of surplus contrary to the provisions of said section.

(12) The determination that for the taxable year 1933 petitioner is liable under the alleged authority of Section 104(a) of the Revenue Act of 1932 in the amount of $14,224.80 as a surtax for the alleged accumulation of surplus contrary to the provisions of said section. [35]

(13) The determination that for the taxable year 1934 petitioner is liable under the alleged authority of Section 102(a) of the Revenue Act of 1934 in the amount of $9,740.70 as a surtax for the alleged accumulation of surplus contrary to the provisions of said section.

(14) In making the determinations complained of in assignments 10 to 13 hereof, inclusive, the failure to consider the true earned surplus of petitioner as distinguished from its taxable earnings and profits as determined in the report or memorandum opinion.

(15) In making the determinations complained of in assignments 10 to 13 hereof, inclusive, the failure to make any finding as to what surplus, if any, petitioner had accumulated in each of the taxable years involved.

VI

(16) The determination that for the taxable year 1932 petitioner is liable for a negligence penalty under the alleged authority of Section 293(a) of the Revenue Act of 1932 in the amount of $165.84, when the record does not disclose that any part of the deficiency determined was "due to negligence or intentional disregard of rules and regulations".

(17) The determination that for the taxable year 1933 petitioner is liable for a negligence penalty under the alleged authority of Section 293(a) of the Revenue Act of 1932 in the amount of $785.24, when the record does not disclose that any part of the deficiency determined was "due to negligence or intentional disregard of rules and regulations".

(18) The determination that for the taxable year 1934 petitioner is liable for a negligence penalty under the alleged authority of Section 293(a) of the Revenue Act of 1934 in the amount of $582.63, [36] when the record does not disclose that any part of the deficiency determined was "due to negligence or intentional disregard of rules and regulations".

General

(19) The failure to make comprehensive and generally applicable findings of facts which would apply equally to all issues involved in the proceedings and be adequate for proper determination of all the issues involved.

(20) The setting forth separately in the report or memorandum opinion in connection with the discussion and determination of each of the issues involved therein of inadequate facts to support the conclusions reached in such opinion on the majority of said issues.

(21) The severance of facts in the relation to each of the issues discussed and determined in the report or memorandum opinion so that purported

findings with regard to one issue do not have application to the other issues involved.

(22) The determination of separate issues without regard to facts found to be true with respect to other issues involved in the proceedings.

(N. B. The errors numbered 19, 20, 21, and 22 are manifest from a reading of the report or memorandum opinion on the various numbered issues and from the following express language of the opinion:

"Certain issues as to depreciation upon wooden buildings and automobiles have been settled by stipulation which will be reflected in decision under Rule 50. The other issues will be considered in the order above set forth, the facts, except the general facts as to incorporation stated above, being set forth separately in connection with the discussion of each issue." (Italics supplied.)) [37]

(23) The intermingling of findings of fact, conclusions as to facts and conclusions of law in such manner as to render the decision of the Board in its report or memorandum opinion arbitrary and theoretical.

(24) In making its findings of fact and conclusions of law therefrom the Board failed to make findings of fact in conformance with the evidence.

Wherefore, the petitioner prays that the decision of the United States Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit; that a transcript of

the record be prepared in accordance with law and the rules of said Court for filing, and that appropriate action be taken to the end that the errors complained of herein be reviewed and corrected by said Court.

WILSON BROS. & CO.,
By FRANCIS A. WILSON
President.

ADOLPHUS E. GRAUPNER,
LOUIS JANIN
Counsel for Petitioner
1110 Balfour Building,
San Francisco, California. [38]

State of California,
City and County of San Francisco.—ss.

Francis A. Wilson being first and duly sworn says, I am president of Wilson Bros. & Co., the petitioner and appellant above-named; that I have read the foregoing petition for review and know the contents thereof and the facts set forth therein are true as I verily believe; that said petition is filed in good faith and not for purposes of delay.

FRANCIS A. WILSON

Subscribed and sworn to before me this 24th day of October, 1940.

[Seal] ELEANOR J. SMITH
Notary Public in and for the City and County of San Francisco, State of California.

My commission expires Dec. 31, 1943.

[Endorsed]: U.S.B.T.A. Filed Oct. 31, 1940. [39]

[Title of Board and Cause.]

Docket No. 83,397

AFFIDAVIT OF SERVICE BY MAIL

Louis Janin, being first duly sworn, deposes and says:

That he is a citizen of the United States, and over the age of 21 years, and not a party to the above-entitled proceedings. That on this 30th day of October, 1940, he deposited in the United States Post Office in San Francisco, California, addressed to the Commissioner of Internal Revenue, Internal Revenue Building, Washington, D. C., a copy of petition for review in the above-entitled proceedings, together with a notice of mailing petition for review, addressed to said Commissioner of Internal Revenue, and to John P. Wenchel, Chief Counsel, Attorney for Commissioner. That said copy of petition and notice of filing petition were enclosed in an envelope addressed to the Commissioner of Internal Revenue, Internal Revenue Building, Washington, D. C., with air mail postage prepaid thereon for immediate and prompt delivery.

LOUIS JANIN

Subscribed and sworn to before me this 30th day of October, 1940.

[Notarial Seal] EDITH VIA

Notary Public in and for the City and County of San Francisco, State of California.

[Endorsed]: U.S.B.T.A. Filed Oct. 31, 1940. [40]

[Title of Board and Cause.]

To Commissioner of Internal Revenue, and to John P. Wenchel, Chief Counsel, Attorney for Respondent, Bureau of Internal Revenue Building, Washington, D. C.:

You are hereby notified that on this 31st day of October 1940, a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit, of the decision of the United States Board of Tax Appeals, heretofore rendered in the above-entitled cause, was mailed by air mail to the Clerk of said Board. A copy of the petition as filed is attached hereto, and served upon you.

Dated: This 30th day of October, 1940.

(s) ADOLPHUS E. GRAUPNER
(s) LOUIS JANIN
Attorneys for Petitioner.

Service of the foregoing notice of filing and of a copy of the petition for review is hereby acknowledged this 31st day of October, 1940.

(s) J. P. WENCHEL
Chief Counsel, Bureau of Internal Revenue
Attorney for Respondent.

[Endorsed]: U.S.B.T.A. Filed Nov. 1, 1940. [41]

[Title of Board and Cause.]

STATEMENT OF POINTS ON WHICH PETITIONER INTENDS TO RELY

In compliance with paragraph (d) of Rule 75 of the Rules of Civil Procedure for the District Court of the United States Board of Tax Appeals by Rule 30 of the Rules of the United States Circuit Court of Appeals for the Ninth Circuit the above-named petitioner herewith states the points on which it intends to rely on the pending petition for review of the decision of said Board in the above-entitled proceeding.

Petitioner will rely upon all of the assignments of error set forth in the petition for review of decision in the above-entitled proceedings by the United States Circuit Court of Appeals for the Ninth Circuit filed with the United States Board of Tax Appeals on October 31, 1940.

With respect to the above-entitled proceeding involving the taxable calendar years 1932 and 1933 a concise statement of the points involved in the appeal is as follows: [42]

1. The Board of Tax Appeals erred in failing to allow petitioner a valuation, as a basis for depreciation on the Steamship "Idaho" from January 1, 1932 of the amount of $91,377.78 and to determine that petitioner was entitled to deduct depreciation on said steamship for each of the taxable years 1932, 1933 and 1934 in the amount of $6,100.78 per annum. Such error resulted from failure to determine as a part of the basis of depreciation,

the amount of $79,000 as the fair market value of a twenty per cent interest in said steamship given to Mary H. Wilson on February 6, 1917, and by her donated to petitioner on January 2, 1929.

2. The Board of Tax Appeals erred in finding with respect to all the taxable years involved, viz: 1932, 1933 and 1934, as follows:

> "We hold that the petitioner was availed of in the taxable years for the purpose of preventing imposition of surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed."

and further erred in determining that for the year 1932 petitioner is liable under Section 104(a) of the Revenue Act of 1932 for $3,316.84 as a surtax for alleged accumulation of surplus; also, it further erred in determining that for the year 1933 petitioner is liable under the aforesaid section for $14,224.80 as a surtax for alleged accumulation of surplus.

In making such determinations the Board failed to consider petitioner's true earned surplus as distinguished from its taxable earnings and profits as determined in the report or memorandum opinion and, also, failed to make any findings as to what surplus, if any, petitioner had accumulated in each of the taxable years involved. [43]

3. The Board erred in determining that for each of the taxable years 1932 and 1933 petitioner is liable for a negligence penalty under Section 293(a)

of the Revenue Act of 1932 when the record does not disclose that any part of the deficiency determined in each of said years was "due to negligence or intentional disregard of rules and regulations."

4. The Board erred in failing to make comprehensive or general finding of facts applicable to all issues involved and further erred in segregating and separating the findings made so that findings made on one issue, although properly material and applicable to other issues, are made inapplicable to other issues to which they are material and controlling as is evidenced by the following preliminary statement in the report or memorandum opinion:

> "Certain issues as to depreciation upon wooden buildings and automobiles have been settled by stipulation which will be reflected in decision under Rule 50. The other issues will be considered in the order above set forth, *the facts,* except the general facts as to incorporation stated above, *being set forth separately in connection with the discussion of each issue.*" (Italics supplied.)

The Board further erred in failing to make findings of fact in conformance with the evidence, and in intermingling, as findings of fact, facts, conclusions as to facts, and conclusions of law in such manner as to conflict with the record and the law.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for Petitioner.

Admission of service of the foregoing statement of points on which petitioner intends to rely is hereby admitted this 11th day of March, 1941.

J. P. WENCHEL

Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent on Review.

[Endorsed]: U.S.B.T.A. Filed Mar. 11, 1941. [44]

U. S. Board of Tax Appeals Filed March 14, 1941
In The United States Circuit Court of Appeals
For the Ninth Circuit
B. T. A.

Docket No. 83397

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.,) a corporation,
Petitioner on Review,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

B. T. A.

Docket No. 93668

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.,) a corporation,
Petitioner on Review,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

ORDER FOR CONSOLIDATION OF THE RECORD

Upon consideration of the motion filed herein by counsel for the petitioner on review in the above-entitled proceedings, moving the Court to consolidate said proceedings for purposes of record, briefing, hearing and decision, and for other purposes, it is this 10th day of March, 1941

Ordered that the said motion be and it is hereby granted.

And it is further ordered that a certified copy of [45] the motion and this order be transmitted by the Clerk of this Court to the Clerk of the United States Board of Tax Appeals.

(s) CURTIS D. WILBUR
U. S. Cricuit Judge.

[Endorsed]: Filed March 10, 1941. Paul P. O'Brien, Clerk.

A true copy
Attest: March 10, 1941
[Seal] PAUL P. O'BRIEN
Clerk.
By FRANK A. SCHMID,
Deputy Clerk

[Endorsed]: U.S.B.T.A. Filed March 14, 1941. [46]

[Title of Board and Cause.]

DESIGNATION OF CONTENTS OF RECORD ON APPEAL

In compliance with the provisions of paragraph (a) of Rule 75 of the Rules of Civil Procedure for the District Courts of the United States as made applicable to review of a decision of the United States Board of Tax Appeals by Rule 30 of the Rules of the United States Circuit Court of Appeals for the Ninth Circuit, the above-named petitioner hereby designates the portions of the record,

proceedings, and evidence to be contained in the record on review of the above-entitled proceedings, as follows:

1. Docket entries of the proceedings before the Board of Tax Appeals.

2. Motion for order and order granting leave to file amended petition.

3. Amended petition filed July 10, 1939.

4. Answer to amended petition filed July 31, 1939. [47]

5. Stipulation of facts filed in the proceeding, excepting therefrom copies of bills of sale of enrolled vessels attached thereto and referred to as Exhibits A and B to said stipulation.

6. Findings of fact and memorandum opinion of the Board promulgated May 22, 1940.

7. Decision of the Board of Tax Appeals entered August 6, 1940.

8. Petition for Review of Decision of the Board by the United States Circuit Court of Appeals for the Ninth Circuit, filed October 31, 1940.

9. Notice of filing of petition for review and admission of service thereof.

10. Orders enlarging time for preparation, transmission and delivery of the record.

11. Revised Statement of the Evidence.

12. Designation of contents of record on appeal.

13. Statement of Points on which petitioner intends to rely.

14. Petitioner's Exhibits 3, 4, 5, 6, 7, 8, 9, 10, 11, 18, 19, 20, 21, 22 and 23 and Respondent's Exhibits A, B and C.

15. Order of the United States Circuit Court of Appeals, Ninth Circuit, for consolidation of the record.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Counsel for Petitioner,
1110 Balfour Building,
San Francisco, California.

Service of the foregoing designation of the contents of record on appeal is hereby admitted and agreed to this ..... day of March, 1941.

J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent on Review.

[Endorsed]: U. S. B. T. A. Filed March 11, 1941.

[48]

[Title of Board and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 48, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of

Tax Appeals, at Washington, in the District of Columbia, this 20th day of March, 1941.

[Seal] B. D. GAMBLE
Clerk,
United States Board of Tax Appeals.

[49]

[Endorsed]: No. 9782. United States Circuit Court of Appeals for the Ninth Circuit. Wilson Brothers and Company (Wilson Bros. & Co.,) a corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed March 31, 1941.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In The United States Circuit Court of Appeals
For the Ninth Circuit
No. 9782
B. T. A.

Docket No. 93668

WILSON BROTHERS AND COMPANY,
(Wilson Bros. & Co.,) a corporation,
Petitioner on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

NOTICE OF ADOPTION OF DESIGNATION OF CONTENTS OF RECORD AND STATEMENT OF POINTS FILED WITH THE BOARD OF TAX APPEALS.

To the Honorable Justices of the United States Circuit Court of Appeals for the Ninth Circuit:

Notice is hereby given that the Petitioner on Review in the above entitled proceedings hereby adopts for the purposes of petition on review to the above entitled court, the Designation of contents of Record and Statement of Points filed with the Clerk of the United States Board of Tax Appeals in the above numbered proceedings on March 11, 1941.

Dated this 16th day of April, 1941.

ADOLPHUS E. GRAUPNER
LOUIS JANIN
Attorneys for the Above Named Petitioner.

[Endorsed]: Filed April 17, 1941. Paul P. O'Brien, Clerk.

Nos. 9781 and 9782

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

WILSON BROTHERS AND COMPANY (Wilson Bros. & Co.) (a corporation),
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S OPENING BRIEF.

ADOLPHUS E. GRAUPNER,
LOUIS JANIN,
Balfour Building, San Francisco,
Counsel for Petitioner.

PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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Nos. 9781 and 9782

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

WILSON BROTHERS AND COMPANY (Wilson Bros. & Co.) (a corporation),
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S OPENING BRIEF.

I. THE STATUTORY PROVISIONS FOR JURISDICTION.

These consolidated appeals involve income taxes and delinquency penalties for the taxable years 1932, 1933 and 1934, as follows:

	Tax	Delinquency Penalty	Total
1932	$ 3,316.84	$ 165.84	$ 3,482.72
1933	15,724.73	786.24	16,510.97
1934	11,652.75	582.63	12,235.38
Totals	$30,694.32	$1,534.71	$32,229.07

and are taken from the decisions of the United States Board of Tax Appeals entered August 6, 1940. (R. 68, 231.)

Petitions were filed by Wilson Bros. & Co., the petitioner herein with the United States Board of Tax Appeals in each of the proceedings herein involved within ninety days after the respective deficiency notices were mailed to petitioner (R. 1, 203), viz.: petition in Docket No. 83,397 was filed March 25, 1936, that in Docket No. 93,667 was filed May 21, 1938.

The petitions for review in the two appeals involved were filed with the United States Board of Tax Appeals October 31, 1940 (R. 69, 232), pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code. The two cases were ordered consolidated by this Court for purposes of record, briefing, hearing and decision (R. 195, 250) with a complete transcript of the record to be filed only in case No. 9781, which of itself only concerns the taxable year 1934. Therefore to be included in the decision by this Court will be case No. 9782 which is printed in skeleton form in the Transcript (R. 195) and which includes the taxable years 1932 and 1933.

Orders enlarging time within which to transmit, prepare and file the records on appeal in the two cases were duly made by this Court and transmitted to the United States Board of Tax Appeals.

Petitioner is a corporation organized under the laws of the State of Nevada, having, during the taxable years involved, its offices in the City of Reno, Nevada, and the City and County of San Francisco, California (R. 33), and filed its income tax returns for all years involved with the Collector of Internal Revenue, First California District.

II. STATEMENT OF THE CASES.

The petitions involved apply only to such parts of the decisions rendered as are covered by the hereinafter numbered issues stated in the memorandum report or opinion of the United States Board of Tax Appeals, viz.: III(a) and (c) (R. 37, 40), IV(a) (R. 41), V (R. 54) and VI (R. 67). These bring before the Court the following questions: (1) The right of petitioner to deduct amounts charged off as partial bad debts and deducted for the year 1934; (2) The right of petitioner to deduction of additional depreciation on the steamship "Idaho" for all three years; (3) Whether petitioner is liable under section 104 of the Revenue Act of 1932 and section 102 of the Revenue Act of 1934 for surtax for accumulation of surplus; (4) Whether petitioner is liable for a five per cent negligence penalty for each of the three years under section 293(a) of the Revenue Acts of 1932 and 1934, and (5) Whether the Board by subdividing its findings of fact to apply to separated issues and not having general findings of fact which would apply to all issues to which they were material did not grossly err in its decisions. To the foregoing questions the following statement of material facts will be confined.

III. STATEMENT OF FACTS.

1. Prior to the organization of petitioner and on January 31, 1927, F. A. Wilson and W. T. Wilson formed a copartnership to engage in the lumber and shipping business under the name of Wilson Bros. &

Co., which continued to do business under that name until after the formation of the petitioner corporation with the same name, when said copartnership was dissolved in January, 1929. (R. 23, 33.) The two brothers had been continuously and actively engaged in the lumber business since 1906. (R. 88.)

2. Petitioner, Wilson Bros. & Co. (erroneously entitled as Wilson Brothers and Company in the deficiency notices in the proceedings involved (R. 32) is a corporation organized under the laws of the State of Nevada, December 14, 1928, with office in Reno, Nevada, and its principal office in San Francisco, California, during the taxable years involved. The corporation was organized by F. A. Wilson and W. T. Wilson, brothers and partners in the above-described partnership, with an authorized capital stock of 200,000 shares of a par value of $25.00 per share to take over and continue the business of said copartnership. Each of the brothers purchased 20 shares of said capital stock, each paid the petitioner $500.00 therefor, and no other shares have ever been issued. (R. 24, 33.)

3. During the taxable years petitioner kept its books of account on the accrual system and filed income tax returns with the Collector of Internal Revenue for the First District of California. (R. 33, 89.)

4. Petitioner corporation was organized to take over the business of the copartnership, to acquire, own and operate timber lands, to engage in the logging business, the manufacture and transportation of lumber, the operation of steamships as a part of the

logging and lumber business, the buying and selling of lumber, and engaging in the general lumber business. (R. 35, 36, 55, 60, 88.)

5. There was never any intention on the part of the two stockholders that the corporation was to be organized as a holding investment company (R. 55, 60) or that it was to be availed of for the accumulation of surplus or avoidance of surtax on the shareholders. There was never any discussion between or decision by the two stockholders concerning any element of taxation as a reason for forming the corporation or its subsequent failure to pay dividends during the years from its formation through the taxable years involved. (R. 88, 103.)

6. When the corporation was formed the inflated prosperity of late 1928 and early 1929 held sway and petitioner's stockholders had great expectations for petitioner's future. By July of 1929 the impending crash of October, 1929, had so effected the lumber industry that petitioner was forced to "lay up" the three steamships which it operated because their operation ceased to be profitable. (R. 60, 94, 100.) However, at no time from the formation of the corporation through the taxable years involved did the stockholders abandon their plan to enlarge petitioner's business by engaging in logging, lumbering, and shipping, which required larger capital than that represented by the net assets of petitioner. (R. 35, 36, 100-103.)

7. The books of account of petitioner were kept on a simple basis and consisted of journal, ledger, sales books and bank books. Instead of a cash book, bills

were sent out in duplicate and, when a customer paid, one of the copies was kept by petitioner as a record of payment. Such payments were entered in the ledger and the payment was deposited in bank. This system of accounting sufficiently reflected the business transactions of the corporation to the satisfaction of the stockholders. (R. 89, 117.) In the balance sheets made up by the corporation, including those in the income tax returns for the taxable years involved, the cash on hand was incorrectly overstated and did not correspond with the cash position shown in the ledger for the years involved. (R. 90.) These differences between the amounts shown in the ledger and in the balance sheets, including those shown in the returns, arose from a peculiar custom of the two stockholding brothers. From year to year each of the brothers without any consideration whatsoever therefor would place in the cash box of the corporation an I.O.U. for considerable and equal amounts and which they considered the equivalent of cash and called "cash". Those I.O.U.'s did not represent any money borrowed from the corporation and the purpose of putting them into the cash box was to stimulate the brothers to pay them up and produce "a good sized corporation" and at the same time to show (to themselves) large assets. From time to time each of the brothers made contributions on the I.O.U's. Such contributions were deposited in bank and the amounts were then entered in the corporation's books. The existing I.O.U.'s were then destroyed and new ones for smaller amounts were inserted in their place. Such strange custom threw the books of account out of balance with the cash

position shown on the trial balances on the income tax returns and incorrectly indicated a large capital or paid-in surplus in the hands of the corporation. The misstatement of the cash position in the income tax returns did not affect petitioner's taxable income or earned surplus for the years involved in these cases. (R. 91, 117.)

8. When the above-mentioned partnership was dissolved after the organization of petitioner corporation, the partners transferred all their interests in the partnership, excepting accounts receivable and payable, to petitioner. In addition, and over and above the $1000.00 subscribed for shares of stock, the two stockholders contributed assets consisting of cash, stocks in domestic corporations, interests in steamships, land buildings and furniture and fixtures, which, with certain gifts to the corporation by their mother (R. 27, 30, 93) had a book value of $696,000.00. (R. 181, Schedule K, Respondent's Exhibit A.) The cash contributed was, with the exception of a small amount required for operating expenses, used for the purchase of securities.

9. The contributions in cash after the organization of the corporation and down through the years herein involved, were made in equal amounts by each of the stockholders as follows: During the latter part of 1929, $50,000.00; during January, 1930, $54,000.00; and during 1931, $480,312.24, which the brothers had on deposit in the San Francisco Bank. (R. 58, 62, 109.)

10. On the organization of petitioner corporation Mary H. Wilson, the mother of F. A. Wilson and

W. T. Wilson, donated to the corporation, without any consideration to her, a 55/100ths interest in the steamship "Idaho" (R. 27, 43) and also a 10/32nds interest in the steamship "Oregon". (R. 30, 45.) Both of said donations were made on January 2, 1929. Each of F. A. Wilson and W. T. Wilson individually owned a 10/100ths interest in the steamship "Idaho" and an 11/32nds interest in the steamship "Oregon" which had not formed a part of the partnership assets but were contributed by them to petitioner on January 2, 1929. (R. 93.) The value of these steamship interests was set up on the books of the corporation at $175,000.00. (R. 181.)

11. The history of the steamship "Idaho", until the interests of Mary H. Wilson, F. A. Wilson and W. T. Wilson passed to the petitioner corporation on January 2, 1929, is set forth in paragraph 13 of the Stipulations of Facts (R. 26) and is of importance because of the issue relating to the proper amount of depreciation to be allowed petitioner on the vessel. When on February 16, 1917, Henry Wilson, husband of Mary H. Wilson and father of F. A. Wilson and W. T. Wilson, gave his wife a 20/100ths interest in the steamship and each of his sons a 5/100ths interest, the steamship had a fair market value of $395,000.00. (16 B. T. A. 1284, Memorandum Opinion in these proceedings, R. 48.) In 1917 the fair market value of a fractional interest in a vessel was its proportionate part of that of the total value. (R. 48, 106.)

12. In addition to owning the steamship interests mentioned above, petitioner managed and was disburs-

ing and collection agent for the steamship "Svea". (R. 38, 39.)

13. During the taxable years involved petitioner carried on and conducted its lumber business to such extent as could be done under the conditions resulting from the economic and financial depression existing during said years. (R. 56, 88, 102.)

14. Petitioner corporation declared no dividends during the taxable years 1932, 1933 and 1934 herein involved because the profits of the petitioner were not believed to be sufficient to warrant dividends, were desired for future expansion purposes, and the value of its assets, as compared with the costs thereof, were impaired. (R. 101.) The failure to declare dividends was not because of a plan by the brothers to avoid individual taxes. (R. 103.) The two stockholders and officers of the corporation, F. A. Wilson, president, and W. T. Wilson, secretary-treasurer, drew no salaries, for the same reasons they did not have petitioner pay dividends. (R. 61.)

15. The assets and particularly the securities were being conserved because the two stockholders had never abandoned their original idea of enlarging the business by re-entering the logging, lumbering and milling business, which according to their estimate would require fully a million and a half dollars. (R. 101, 102.) The securities were acquired and held by the corporation in order to have liquid assets which would enable them to raise cash quickly and buy anything the stockholders selected for the enlargement of their business. (R. 102.)

16. During the year 1934 petitioner claimed certain deductions for partially worthless debts, which it charged off on the direct write-off method in the total of $15,144.40, as follows:

Woodhead Lumber Company of California	$5,000.00
Steamship "Svea"	4,644.40
Kentucky Fuel and Gas Corporation bonds	5,500.00

These deductions were denied in part III of the memorandum opinion. (R. 32, 37, 94.)

(a) The partial write-off and claimed deduction of $5000.00 as a partially worthless bad debt of the Woodhead Lumber Company of California resulted after the corporation had transferred its going business to another corporation and had remaining assets of such dubious character and value that, after investigation made by the Secretary-Treasurer of petitioner, it was determined that at least $5000.00 of the debt owing petitioner could not be recovered. (R. 95.)

(b) In 1933 petitioner wrote off as a partial bad debt owing from the owners of the wooden steamship "Svea" the amount of $2160.80 and in 1934 it similarly wrote off the amount of $4644.40, which amounts were claimed respectively as deductions in petition's returns for the years mentioned. The petitioner owned no interest in the "Svea" but was managing, disbursing and collection agent therefor. On January 1, 1933, accounts receivable from the "Svea" amounted to $9081.78 and on January 1, 1934, to $10,804.01. The vessel was owned by many small owners who expected petitioner to make the necessary advances to keep the boat in condition to be main-

tained in condition, which it was bound to do and did. Petitioner could anticipate repayment only from earning or recovery from the many owners. As the vessel had not been operated for several years there were no earnings from which to recoup and in 1933 their attorney advised them that a suit to recover would be inadvisable, while in 1934 it appeared that the vessel could not be placed in operation for some time. (R. 38.)

(N. B. While petitioner admits that the accounts receivable from the "Svea" were not proven deductible for normal income tax purposes it will later contend that such accounts must be reduced by their actual value in determining the amount of petitioner's earned surplus and annual earnings available for dividends.)

(c) On January 1, 1934, petitioner was the owner of first lien s.f. 6½ A Bonds of the Kentucky Fuel and Gas Corporation due 1942, having a par value of $43,000.00 acquired as follows:

$18,000.00	par value acquired before January 1, 1932 at a cost of	$9,000.00
$15,000.00	par value acquired during the year 1932 at a cost of	450.00
$10,000.00	par value acquired during the year 1933 at a cost of	20.00
$43,000.00	total par value having a cost on January 1, 1934, of	$9,470.00

(R. 127, 170.) On December 31, 1934, when the petitioner wrote off the amount of $5500.00 as a partially bad debt on account of said bonds and thereafter

claimed that amount as a deduction in its income tax return for the year 1934, the market quotations on the basis of a $100.00 bond as of December 31, 1934, show $4.50 bid and $6.00 asked. (R. 128.) At that time the company was in receivership and it appeared that petitioner would at least take a loss in the amount charged-off. (R. 96.) At December 31, 1934 on "bid basis", the bonds were worth only $1935.00 and on an "asked" basis they were worth $2580.00, while, on the value for partial deduction taken by petitioner there remained as an asset value for said bonds the amount of $3970.00, which was in excess of both the "bid" and "asked" valuations.

17. During the taxable years involved, for which the Board of Tax Appeals held that petitioner was availed of for the purpose of preventing imposition of surtax upon its shareholders (R. 67), W. T. Wilson paid about $150.00 Federal income tax in 1932 and none in 1933 and 1934, while F. A. Wilson, the other stockholder, paid no tax for any of the three years. (R. 59.)

IV. SPECIFICATION OF ERRORS RELIED UPON.

Errors are specified in abbreviated form in the order in which they were assigned in the petitions for review of the two proceedings before the United States Board of Tax Appeals (R. 69, 232) and are arranged to cover in one statement the errors alleged to warrant review and partial reversal of the decisions of the Board based upon the consolidated re-

port or memorandum opinion of the Board (R. 31) for the three taxable years involved, viz.:

1. The Board erred in failing to find and determine that the $43,276.06 account receivable due from the Woodhead Lumber Co. of California was impaired during the year 1934 in the amount of $5000.00, as charged off and deducted by petitioner for said year as a partial bad debt, and that petitioner was entitled to a deduction for said year of said $5000.00. (R. 73, 237.)

2. The Board erred in failing to find and determine that the cost of bonds of the Kentucky Fuel Gas Corporation owned by petitioner was impaired in value during the year 1934 in the amount of $5500.00, as charged off and deducted by petitioner for said year as a partial bad debt, and that petitioner was entitled to a deduction for said year of said amount of $5500.00. (R. 74, 237.)

3. The Board erred in failing to find and determine that petitioner was entitled to deduct for each of the three taxable years involved the amount of $6100.77 per annum for depreciation on the steamship "Idaho" and to allow a value as a basis of depreciation from January 1, 1932, in the amount of $91,337.78. It further erred in failing to allow petitioner, as a part of the basis of depreciation of said steamship "Idaho" from January 1, 1932, the amount of $79,000.00 as the fair market value of a twenty per cent interest therein given to Mary H. Wilson on February 6, 1917, by her husband, when said steamship had a total fair market value of

$395,000.00, which said twenty per cent interest was donated to petitioner by said Mary H. Wilson on January 2, 1929. (R. 75, 238.)

4. The Board erred in finding and determining with respect to all of the taxable years involved and without discrimination or distinction between and contrary to the circumstances and facts relating to the several years 1932, 1933 and 1934 that petitioner was availed of in each of said taxable years for the purpose of preventing imposition of surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed. The Board erred in determining that for the taxable years 1932 and 1933 petitioner was liable for the respective amounts of $3316.84 and $14,224.80 as surtaxes for the alleged accumulation of surplus during each of said years contrary to the provisions of section 104(a) of the Revenue Act of 1932. It further erred in determining that for the taxable year 1934 petitioner was liable for the amount of $9740.70 as a surtax for the alleged accumulation of surplus contrary to the provisions of section 102(a) of the Revenue Act of 1934. (R. 75, 76, 239, 240.)

5. The Board erred in finding and determining that for each of the taxable years involved petitioner was liable for a five percentum negligence penalty under section 293(a) of the Revenue Acts of 1932 and 1934. (R. 77, 240.)

6. The Board erred in not making its findings of fact comprehensive and general so that, where

material, they would apply equally to and be adequate for the proper determination of all the issues involved. The Board further erred in separating and severing its findings of fact under separate and independent issues in its report or memorandum opinion and thus making facts of material general import applicable only to one issue when they should have been made applicable to other issues to which they were also material. (R. 78, 241.)

7. The Board erred in intermingling findings of facts, conclusions of fact and conclusions of law in the several subdivisions of its report or memorandum opinion so as to render the decisions based thereon arbitrary and erroneous in law and fact. (R. 79, 242.)

8. The Board erred in not making its findings of fact and conclusions of law conform to the evidence. (R. 79, 242.)

V. ARGUMENT OF THE CASES.

1. THE BOARD ERRED IN DETERMINING THAT PETITIONER WAS NOT ENTITLED TO DEDUCT FROM THE ACCOUNT RECEIVABLE DUE IT FROM THE WOODHEAD LUMBER CO. OF CALIFORNIA THE AMOUNT OF $5000.00 AS A PARTIAL BAD DEBT WHICH IT HAD WRITTEN OFF AND DEDUCTED FOR THE TAXABLE YEAR 1934.

The partial write off made and deduction claimed against the Woodhead Lumber Co. of California in the amount $5000.00 for the year 1934 was disposed of in the deficiency notice by the following explanation:-

> "2. The bad debts have been disallowed in accordance with section 23(k) of the Revenue

> Act of 1934 for the reason no evidence has been submitted to establish the worthlessness thereof and no permission has been granted you to change from the actual bad debt basis elected in prior years to the reserve basis." (R. 17.)

The second clause of the explanation refers to respondent's claim that the partial deduction was not a write-off but a transfer to a reserve for bad debts, which transfer could not be made without permission granted by the Commissioner. (Regulations 86, Art. 23(k)-1-(2).) However, this part of respondent's explanation and claim is entirely erased by the report or memorandum opinion of the Board wherein it is found that: "The petitioner was on the actual charge-off method of deducting bad debts" (R. 37), and consequently did not use the method of transfer to reserves for bad debts.

Section 23(k) of the Revenue Act of 1934 which relates to the deduction from gross income of bad debts, reads as follows:

> "(k) *Bad Debts*—Debts ascentained to be worthless and charged off in the taxable year * * *; and when satisfied that a debt is recoverable only in part, the Commissioner may allow such debt, in an amount not in excess of the part charged off within the taxable year, as a deduction."

The allowance by the Commissioner of the partial deduction of a bad debt is to be found in Regulations 86, Art. 23(k)-1-(2) where it is provided.:

> "If all the surrounding and attending circumstances indicate that a debt is worthless,

> either wholly or *in part, the amount which is worthless and is charged off* or written down to a nominal amount on the books of the taxpayer *shall be allowed* as a deduction in computing net income." (Italics supplied.)

With regard to the deduction of $5000.00 as a partially worthless debt of the Woodhead Lumber Co. of California, it may be said that that part of the report or memorandum opinion which refers thereto (R. 37, 38) is confused, incorrect, and erroneous. The uncontradicted facts which show this follow.

On January 1, 1934, and throughout that year, petitioner had accounts receivable from the Woodhead Lumber Co. of California amounting to $43,276.06. On December 31, 1934, petitioner wrote-off $5000.00 of the total accounts receivable from that company as a partial loss and in its income tax return for 1934 deducted that amount from its gross income as a partial bad debt. (R. 37.)

In 1932 the Woodhead Lumber Co. of Nevada bought the inventory and some of the physical assets of the Woodhead Lumber Co. of California in consideration of its promissory note for $25,000.00 and, as collateral, $37,000.00 par value of its capital stock. The California corporation turned over to petitioner as security for its indebtedness of $43,276.06 the note for $25,000.00, secured by $37,000.00 par value stock of the Nevada corporation, which stock petitioner did not believe to have a value of $37,000.00. (R. 38, 39.) The face value of the $25,000.00 note only may be considered as the maximum value of the pledge.

During 1934 the secretary-treasurer of petitioner went to Los Angeles and went over the books and affairs of the Woodhead Lumber Co. of California to ascertain its financial condition. He found that books of the company disclosed that "it was in very bad shape"; that there was a heavy mortgage on the assets; that there was a bond issue of about $200,000.00 on a specific piece of land and that the bonds and interest rights preceded those of general creditors, of which petitioner was one; that the improvements and lumber business of the corporation were located on rental property which was held on a month to month basis and that if the corporation was thrown off that property the improvements thereon would become practically worthless; and that the balance of the assets of the corporation consisted of accounts receivable which he judged "were no good". After careful examination of the books of the California corporation, the secretary-treasurer of petitioner determined that with the best advantage to that corporation, petitioner would lose at least $5000.00 and therefore wrote that amount off the corporation's books in 1934 as being a reasonable deduction for partial loss. Petitioner never recovered the $5000.00 which it deducted, and the affairs of the Woodhead Lumber Co. of California continued to grow steadily worse. (R. 95.)

The foregoing supplies the evidence of partial worthlessness which respondent apparently lacked or never sought when he made his explanation of reasons for denying the deduction. (*Supra.*) Other than that statement in the deficiency notice, there is

no plea or proof of defense of respondent's denial of the deduction.

Conceding that the promissory note of the Nevada corporation which had been turned over to petitioner by the California corporation as security was worth its face value, the status of the account receivable of petitioner from the California corporation in 1934 was as follows:

Accounts receivable, Woodhead Lumber Co. of California	$43,276.06
Unpaid promissory note for $25,000.00 as security	25,000.00
Balance due petitioner, unsecured	$18,276.06

With the California corporation shown by the uncontroverted evidence recited above to be in a hopeless financial condition, the deduction of $5000.00, less one-third of the $18,276.06, may not be deemed to be an unreasonable write-off and deduction for a partially worthless bad debt. Petitioner has made proof of the "surrounding and attending circumstances" which indicated that the debt of the Woodhead Lumber Co. of California was partially worthless within the intendment of Regulations 86, Art. 23(k)-1-(2) (*supra*) and respondent did not introduce a single item of evidence to prove the contrary. All that respondent did was to attempt to confuse the issues by injecting the dealings of petitioner with the Woodhead Lumber Co. of Nevada. Over this confusion the deciding member of the Board of Tax Appeals seems to have stumbled and made his erroneous decision.

Under part III(a) of the report or memorandum opinion, the Board (R. 37) apparently finds that

there were two deductions sought on the accounts receivable from the Woodhead Lumber Co. of California: (1) $15,144.40 and (2) $5000.00. This is a confusion, for only $5000.00 was sought as a deduction. (R. 95.) It is next found that petitioner was on the actual charge-off method instead of the reserve method of deducting bad debts. (R. 37.) These determinations entirely defeat the Commissioner's reasons set forth in the deficiency notice (*supra*) for disallowing the deductions.

The next finding is that petitioner caused an examination of the affairs of the Woodhead Lumber Co. of California and from resulting disclosures reached the conclusion in 1934 that $5000.00 would be a reasonable amount to write-off and take as a deduction for such alleged partial debt during the year 1934 and such was taken. (R. 37.) There is no finding that the examination made by petitioner was superficial, or that the conclusion reached was unsound, or that the conclusion was not supported and sustained by the examination. (R. 37.) Under such conditions and upon such findings petitioner was entitled to the naturally consequent finding that the $5000.00 was deductible.

Moock Electric Supply Co. v. Commissioner, 41 B. T. A. 1209, 1211.

The findings and conclusions then fall into the confusion raised by respondent at the trial as a smoke-screen of defense. Apparently on the sole ground that petitioner was doing business with the Woodhead Lumber Company of Nevada it is found that the worthlessness of the debt of the Woodhead Lumber

Co. of California, an entirely different entity, has not been shown. (R. 38.) The worthlessness of the debt of the California corporation is a matter separate, its solvency is something apart, and the Board erred in considering anything concerning the Nevada corporation in denying the deduction to petitioner.

The finding and determination of the Board on this issue is not supported by the facts and is clearly erroneous. As stated in *Clark v. Commissioner,* 85 Fed. (2d) 622, 624, (C. C. A. 3.)

> "A taxpayer is expected to be reasonable and honest, but the taxing act does not require him to be an incorrigible optimist; * * * neither should he be 'unduly pessimistic' when claiming deductions for bad debts. He 'must make a reasonable investigation of the facts and draw a reasonable inference from the information thus obtainable'."

The facts show that the petitioner met every requirement of his rule and the determination of the Commissioner and the re-determination of the Board should be reversed.

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2. THE BOARD ERRED IN DETERMINING THAT PETITIONER WAS NOT ENTITLED TO DEDUCT THE AMOUNT OF $5500.00 AS A PARTIAL LOSS OR BAD DEBT RESULTING FROM DEPRECIATION IN VALUE OF BONDS OF THE KENTUCKY FUEL GAS CORPORATION OWNED BY PETITIONER AND WHICH IT HAD WRITTEN OFF AND DEDUCTED FOR THE TAXABLE YEAR 1934.

The explanation for the denial of the deduction found in the deficiency notice and the statutory and regulation provisions applicable are quoted at the

opening of the argument on the preceding point, and will not be repeated.

The gist of the denial of the deduction found in the memorandum opinion of the Board (R. 41) is stated as follows:

> "The record does not show when or from whom the bonds were acquired, the cost, nor whether in 1934 there was a basis for partial charge-off which did not exist in 1933 or earlier."

This premise for affirmation of the Commissioner's denial of the deduction is in part erroneous and in part immaterial assumption. (a) The record does show "when" the bonds were acquired as far as necessary for the purpose of partial deduction: viz. $18,000.00 par value bonds were acquired before January 1, 1932; during 1932 $15,000.00 par value bonds were acquired, and during 1933 $10,000.00 par value bonds were acquired. All that is material as to date of acquisition, viz.: acquisition before 1934, is shown in the record. (R. 127, 170.)

(b) "From whom the bonds were acquired" is entirely immaterial. Such information would not and could not in any way affect the cost, 1934 worth, or depreciated value of the bonds.

(c) "The cost" of the bonds is shown by the record (R. 127) at a total of $9470.00.

(d) "Whether in 1934 there was a basis for partial charge-off which did not exist in 1933 or earlier" is not material to the allowance of a partial charge-off and deduction in 1934. The uncollectible portion of a debt not wholly worthless may be charged off at any

time. The rule which is applicable to a total charge-off and deduction does not apply to a partial write-off and deduction.

Moock Electric Supply Co. v. Commissioner, 1209, 1211.

To close its argument to deny the partial deduction by petitioner on the partial worthlessness of the Kentucky Fuel Gas Corporation bonds in 1934 and to sustain the Commissioner the memorandum opinion cites the bid prices on the bond for only a portion of the years from January 1, 1930 to December 31, 1934, using a fragment of the evidence and ignoring the remainder to bolster its conclusion that there was no error. (R. 41.)

The market values of the bonds were taken from the Bank and Quotation Record (R. 128) and were as follows:

	Bid	Asked
January 1, 1930	$74.00	$79.00
December 31, 1930	35.00	45.00
December 31, 1931	5.00	7.00
December 31, 1932	1.25	4.00
December 31, 1933	2.00	4.00
December 31, 1934	4.50	6.00
December 31, 1935	8.00	
December 31, 1936	18.50	
November 30, 1937	8.00	

When we subtract the bid figures for any of the years from the cost of the bonds to the petitioner we find in each year a balance in excess of the partial deduction sought by petitioner. How then may the Board select any one year, particularly the year 1934, and

determine which year was the proper one in which to take a partial deduction, or to say that 1934 was not the proper year.

This decision of the Board was made despite prior declarations by it of the rights of a taxpayer, viz.:

> "The ascertainment, under the statute, of partial or (total) worthlessness of a debt *is obviously for the petitioner, in the exercise of his best judgment,* first to make. *Dillon Supply Co.,* 20 B. T. A. 404, 409. The facts and circumstances surrounding the petitioner's decision should establish it as that of a prudent person of sound judgment. *Anna Bissell,* 23 B. T. A. 572, 578." (Italics in text supplied.)
>
> *Henry A. Hunting v. Commissioner,* 32 B. T. A. 495, 500.

Furthermore, the finding of no proof was made in the face of uncontradicted testimony of the secretary-treasurer of the corporation that "We made the charge-off because the company went into a receivership and we would not recover the full amount but would take a loss in the amount charged off. I made an investigation through the people who issued the bonds and that was their opinion. I had a list of the assets and liabilities of the corporation and in studying the balance sheet it appeared that 'there (were) certain assets that were O. K. and that there would be some recovery due to that fact.' I discussed the matter with my brother, the other stockholder in the corporation, and we reached the determination that the situation of the Kentucky Fuel & Gas Corporation looked pretty bad and that the amount of

$5500.00 should be written off as there was no way to set it back." (R. 96.)

The foregoing quotation from the record, which was not disputed or overcome by any evidence offered by respondent, clearly shows that petitioner complied with the rule adopted by the Board and cited in *Hunting v. Commissioner, supra.*

The only real attempt of respondent to overcome the position assumed by petitioner in deducting the $5500.00 on account of the partial worthlessness of the first sinking fund 6½% bonds of 1942 of the Kentucky Fuel Gas Corporation bonds which petitioner owned, was to bring out on cross examination the bid and asked prices on the corporation's debentures 6½s of 1938, an entirely different security from that owned by petitioner. (R. 129.) If this testimony is relative or material to the issue involved, it certainly confirms the judgement of petitioner's officers in determining to make the partial write-off and deduction, because it shows a static condition for 1932, 1933 and 1934 of nothing bid and $2.00 asked for such securities.

An accountant testifying for the petitioner stated that in his opinion that a substantial loss of value of the bonds had occurred. Also, that because the bonds owned by petitioner were the senior issue and contained a sinking fund provision, the market quotations were a very definite index of the extent of the impairment of actual value, that is, the amount collectible on such bonds. He further testified that good accounting practice required the write-off of the cost

of these bonds by at least the amount of $5500.00 claimed as a deduction. (R. 127-128.)

It appears that the memorandum opinion (R. 41) apparently assumes that a further downward change in market value of the bonds was necessary in 1934 in order to warrant the partial write-off and deduction. This assumption is contrary to the rule applicable to partial deductions as adopted by the Board and the courts, viz.:

> "And nothing seems to be better settled than the partial worthlessness, as distinguished from total uncollectibility, is a ground for deduction which may be pursued or relinquished by a taxpayer *entirely* at his option. If he fails to take a deduction for partial worthlessness in any year, *it does not have the effect of foreclosing him from a reliance upon different developments at another time. Blair v. Commissioner,* 91 Fed. (2d) 992 (C. C. A. 2d Cir.); See *American Cigarette & Cigar Co. v. Bowers,* 92 Fed. (2d) 596 (C. C. A. 2nd Cir.); *Freeman-Dent-Sullivan Co. v. United States,* 21 Fed. Supp. 972; G. C. M. 18525, 1937-1 C. B. 80, 82." (Italics in text supplied.)
>
> *Moock Electric Supply Co. v. Commissioner,* 41 B. T. A. 1209, 1211.

In view of the foregoing it is respectfully submitted that part III(c) of the report or memorandum opinion of the Board is subject to unqualified reversal.

3. **THE BOARD ERRED IN FAILING TO FIND AND DETERMINE THAT PETITIONER WAS ENTITLED TO DEDUCT FOR EACH OF THE THREE TAXABLE YEARS INVOLVED THE AMOUNT OF $6100.77 PER ANNUM FOR DEPRECIATION ON THE STEAMSHIP "IDAHO" AND TO ALLOW A VALUE AS A BASIS OF DEPRECIATION FROM JANUARY 1, 1932, IN THE AMOUNT OF $91,337.78.**

This issue involves part IV of the report or memorandum opinion of the Board of Tax Appeals (R. 41) and involves but a single question of law. The Board held that the basis of petitioner's 75% interest in the Steamship Idaho, acquired by tranfers to it in 1929 was to be determined for purposes of depreciation as follows:

10/100ths transferred by F. A. and W. T. Wilson...	$ 39,500.00
10/100ths purchased by above brothers and transferred to petitioner	11,716.67
35/100ths transferred by Mary H. Wilson.....	70,000.00
20/100ths transferred by Mary H. Wilson.....	40,000.00
Giving petitioner a total basis (unadjusted) of.....	$161,216.67

The Board further held that the adjustment for depreciation allowed or allowable, with respect to the foregoing interests, was $108,750.00, resulting in an adjusted basis on January 1, 1932 of $52,466.67. (R. 47-51.) As petitioner is in accord with the Board's determination on this issue in all respects, except as to the basis applicable to the 20/100ths interest acquired by Mary H. Wilson as a gift from her husband February 16, 1917, and transferred by her to petitioner in January, 1929, detailed facts applicable to the other interests will be omitted.

The parties are in agreement that the adjusted basis as of January 1, 1932 is subject to a depreciation

allowance of 6⅔%, on a fifteen year remaining useful life. The Board's figures, *supra,* result in an annual allowance of $3497.77 as compared to petitioner's present claim (less than claimed before the Board) of $6097.77.

The dispute as to the basis of the 20/100ths interest transferred by Mary H. Wilson to Petitioner in 1929 is dependent upon the effect to be accorded Section 113 of the Revenue Act of 1928. The facts applicable to the question are stated briefly:

On February 6, 1917, Mary H. Wilson was given a 20/100ths interest in the "Idaho". This interest had a cost of $40,000.00 but on that date had an admitted fair market value of $79,000.00. (R. 48-50.) On January 2, 1929, she contributed this interest to petitioner. Respondent claims the basis to petitioner to be the cost to Mary H. Wilson's donor, or $40,000.00. Petitioner claims the basis to be market value as of February 6, 1917, or $79,000.00. (R. 47-50.)

The Board erroneously quotes and relies solely upon section 113(a)(2) of the Revenue Act of 1932 in making its determination upon this point. (R. 50.) As the transfer was made by Mary H. Wilson in January, 1929, the Revenue Act of 1932 has no application. However, the Revenue Act of 1928, provides the applicable statutory provisions and from that we quote.

Section 113(a)(2) of the Revenue Act of 1928 provides:

> "If the property was acquired by gift after December 31, 1920, the basis shall be the same as

it would be in the hands of the donor or the last preceding owner by whom it was not acquired by gifts. * * *"

Section 113(a)(4) of the Revenue Act of 1928, which is highly important and which the Board entirely ignores, reads, as far as material, as follows:

"If the property was acquired *by gift* or transfer in trust *before December 31, 1920, the basis shall be the fair market value of such property at the time of such acquisition.*" (Italics supplied.)

These subsections find their inception in Section 202(a) of the Revenue Act of 1921, which Section, in so far as material, provides:

"(2) In the case of such property acquired by gift after December 31, 1920, the basis shall be the same as that which it would have in the hands of the donor or the last preceding owner by whom it was not acquired by gift. * * *"

* * * * * * *

"In the case of such property acquired by gift *on or before December 31, 1920, the basis* * * * *shall be the fair market value* of such property at the time of such acquisition." (Italics supplied.)

The second paragraph of the quotations from section 202 (a)(2) was put into the act to specify existing law. *Seideman's Legislative History,* 784, 785. Therefore the basis of the 20/100ths interest of the Idaho, from February 6, 1917 until Mary H. Wilson parted with it was clearly its value on February 6, 1917, i.e., $79,000.00.

Section 202(a)(2) of the Revenue Act of 1921 was adopted in order to prevent tax evasion. The evasion in question was the result of a simple expedient. A man who had property with a low basis to himself would not sell it when its value was high, he would give it to his wife and she would sell the property. If he had sold it he would have been taxed with the gain. Because the wife's gain was only the difference between the value at the time of the gift and what she received on the sale (practically no difference) and the transaction escaped tax.

Seideman's Legislative History, 784, 785.

The purpose of the amendment was to prevent future evasion. An unsuccessful attempt was made to make the rule retroactive to all gifts after February 28, 1913. The amendment as adopted left the basis of property in the hands of existing donees exactly as it had been before, and did so deliberately.

Seideman's Legislative History, 785.

With this legislative history and purpose in mind it becomes pertinent to consider the language of Section 113(a)(2) of the Revenue Act of 1928, quoted *supra.* The section provides that the basis "shall be the same as it would be in the hands of the *donor or the last preceding owner by whom it was not acquired by gift.*"

If this section ended with the word donor, petitioner's contention would clearly be correct, without consideration of section 113 (a) (4). If it did not contain the words "the donor" respondent's interpretation would have to be sustained, if section

113(a)(4) could be discarded. But the statute actually contains both expressions, and it must be assumed that their inclusion was deliberate rather than accidental, particularly in view of the expressed purpose of the amendment.

If Congress meant that in all cases the basis would be the same as that of the last preceding owner by whom it was not acquired by gift it would have left out the words "the donor" and the congressional intent would be explicit in the language. What was very definitely intended was that the basis of future gifts would not be changed by the making of the gift. It intended only a prospective application of the amendment, not a retrospective application that would change the existing basis.

The addition of the last paragraph in section 202(a)(2) quoted above and its perpetuation in section 113(a)(4) quoted above (which the Board has completely ignored), proves the argument made above.

The absurdity of the construction contended for by respondent may be simply illustrated. Let us assume that the gift to Mary H. Wilson was made four years earlier, on February 6, 1913. Let us further assume that there has been many earlier gifts of the same property, and that the last preceding owner who had paid a full consideration had purchased it in 1800 for $10.00, and that the petitioner sells it in 1942 for $300,000.00. Can the Commissioner ignore the value of the property on February 6, 1913, or March 1, 1913 in measuring taxable income? Under the construction which respondent urges he would be required to find a taxable gain of $299,990.00.

Such a construction is directly opposed to the intent of the words used, the purpose of Congress in enacting the amendment, and the meaning of the word "income". If the statute means what respondent contends it to mean, it is so capricious, illogical, retroactive and unreasonable that it is violative of the Fifth and Sixteenth Amendments to the Constitution.

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4. THE BOARD ERRED IN DETERMINING THAT PETITIONER WAS AVAILED OF IN THE TAXABLE YEARS FOR THE PURPOSE OF PREVENTING IMPOSITION OF SURTAX UPON ITS SHAREHOLDERS THROUGH THE MEDIUM OF PERMITTING ITS GAINS AND PROFITS TO ACCUMULATE INSTEAD OF BEING DIVIDED OR DISTRIBUTED.

No evidence exists in support of the Board's opinion on this issue. All of the evidence supports the business reasons for the failure to pay dividends. Incontrovertible evidence supports the disbelieved positive testimony that the purpose was not to avoid tax on the shareholders. No reason exists for the disbelief of the testimony. The Board's opinion on this issue is arbitrary and irrational.

The Board's decision relates to sections 104(a) of the Revenue Acts of 1932 and 102(a) of the Revenue Act of 1934 which read respectively as follows:

> "SEC. 104. ACCUMULATION OF SURPLUS TO EVADE SURTAXES.
>
> (a) If any corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there shall be

levied, collected, and paid for each taxable year upon the net income of such corporation a tax equal to 50 per centum of the amount thereof, which shall be in addition to the tax imposed by section 13 and shall be computed, collected and paid upon the same basis and in the same manner and subject to the same provisions of law, including penalties, as that tax."

"SEC. 102. SURTAX ON CORPORATIONS IMPROPERLY ACCUMULATING SURPLUS.

(a) *Imposition of Tax.* There shall be levied, collected, and paid for each taxable year upon the adjusted net income of every corporation (other than a personal holding the company as defined in section 351) if such corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders or the shareholders of any other corporation, through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, a surtax equal to the sum of the following:

(a) 25 per centum of the amount of the adjusted net income not in excess of $100,000. plus

(b) 35 per centum of the amount of the adjusted net income in excess of $100,000."

While the two sections above quoted differ in their wording, their purpose is the same.

The Board determined "that the corporation" (petitioner) "was not FORMED for the purpose interdicted by the above sections". (R. 60.) Therefore the issue before the Court is on the alternative: "Was the corporation AVAILED OF during 1932, 1933 and

1934 for the purpose of preventing imposition of surtax upon its two stockholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed?" (R. 61.)

Before discussing the "purpose" of the corporation and the findings of the Board in relation thereto, we desire to call the attention of the Court to the very peculiar arrangement of the report or memorandum decision so that findings are isolated under discussion and determination of certain issues and eliminated where they may be material to the consideration and determination of other issues, such as the one being discussed. This feature constitutes grievous error and, except by condoning the commission of such error, the Board cannot be sustained in its determination that petitioner is liable for surtaxes.

After making general findings as to the formation of a copartnership by F. A. Wilson and W. T. Wilson under the name of Wilson Bros. & Co. on January 31, 1927, and the organization of a corporation under the same name by the two partners on December 14, 1928, the report or memorandum opinion, after stating that certain issues had been settled by stipulation, declares:

> "The other issues will be considered in the order above set forth, *the facts,* except the general facts as to incorporation stated above, *being set forth separately* in connection *with discussion of each issue.*" (R. 33.) (Italics supplied.)

Thus no matter how material a finding of fact may be, it is not to be considered, says the Board, in the

determination of any other issue, unless re-found as applicable to such other issue. A declaration such as this, if sustained, means that a Board or Court can use or exclude testimony and evidence to suit its own purposes or that the petitioner or plaintiff must anticipate what the Board or Court may deem the issues and re-offer his testimony and evidence as being applicable in part or in whole to each of the several and specific issues involved. Such a situation is inconceivable, particularly in tax proceedings where the Commissioner's determinations are presumed to be *prima facie* correct and the burden of proof is placed on the taxpayer.

The findings made by the Board "as material" to the present issue are insufficient, omit important facts, and engage in error. Therefore, we will restate the material facts to accord with the several material findings made by the Board and the uncontradicted evidence applicable to all issues.

Petitioner was organized on December 14, 1928, by F. A. Wilson and W. T. Wilson to continue the business of the partnership. (General Finding, R. 33.) A partnership which was not engaged in logging or manufacturing lumber and owned no ships. (Special findings in issues II and III, R. 36, 43, 45.) Petitioner was organized to engage in the business of logging, manufacture, purchase, sale and transportation of lumber, and operation of steamships. (Special finding on issue V, R. 55.) The two stockholders had been continuously and actively engaged in the lumber business since 1906 (R. 88) and organized the cor-

poration to engage in a much enlarged endeavor. The steamers "Oregon" and "Idaho" were acquired in January, 1929, were operated by the petitioner for about six months and were then laid up, and had not again been put into operation at the close of the taxable years. (Special finding on issue V, R. 56.) The steamers were acquired by petitioner in January, 1929 principally for the purpose of transporting lumber. After acquisition they were operated only five or six months before they were "laid up" because business got so bad that they could not be operated at a profit. *The country then was experiencing a depression which lasted several years.* During the taxable years in issue the steamers were kept in serviceable condition, in order that petitioner might use them if opportunity was afforded to profitably resume lumber transportations. Petitioner *always expected* to put the ships back into commission and re-engage in the shipping of lumber *when conditions became favorable* and the vessels, though not actively in use, were considered a part of the operating assets of the petitioner. (Special finding on issue II wherein deductions for maintenance of the steamships were sustained. R. 35 and 36.)

During the taxable years involved some lumber and allied business was carried on. The corporation *always had the purpose* of re-engaging in the lumber and shipping business, but did not re-enter the logging, lumbering and milling business during the taxable years, *which would have required a capital of about $1,500,000.00,* because losses were then heavy in the logging and sawmill business, business *was de-*

pressed, no building was going on, it was hard to sell lumber, and it would have been unprofitable to go into a business which then was losing money. (Special findings on issue V, R. 56.) The record shows that approximately $1,500,000.00 or more would be required to re-enter the logging, lumbering and milling business (R. 101) and petitioner did not have this amount in cash or securities in any of the taxable years. (R. 58.)

After the formation of the corporation and during the years 1929, 1930 and 1931, in addition to the original assets set up on the books at a value of $696,000.00, capital cash contributions were made to petitioner by its two stockholders in equal amounts in total as follows: during 1929, $50,000.00; during 1930, $54,000.00; and during 1931, $480,312.24. During the taxable years, no capital contributions were made. (Statement of evidence, R. 109.) With such contributions of cash the petitioner purchased securities, in practically all cases stocks of domestic corporations. No stocks or bonds were transferred by the stockholders to petitioner. (Special findings on issue V, R. 57.) The Board found (Special findings on issue V, R. 61) that contributions by the stockholders included "large amounts of cash" made during the taxable years involved. The contributions of the stockholders were principally made prior to 1932 (R. 109) and the record contains no evidence of any other contributions than those pointed out above.

The securities acquired from all sources, as shown by the books of account and record, had a cost and market value for the taxable years as follows:

December 31, 1932	Cost	$750,943.50	Market value		$439,961.87
December 31, 1933	"	782,190.55	"	"	777,792.00
December 31, 1934	"	837,778.05	"	"	810,797.75

(Special findings on issue V, R. 58.) The securities *were acquired and held* by the petitioner *in order to have liquid assets* for the time when it would go back into the lumber, logging and milling business. They could be sold quickly and provide cash with which to buy anything petitioner wanted. (Statement of evidence, R.102.) At no time did the security investments plus cash on hand equal the $1,500,000.00 required for the proposed enlargement of the business. (R. 58.)

The total cash contributions to capital during 1929, 1930, and 1931 as stated above was $584,312.24. (R. 109.) As respondent's exhibits A, B and C show that for 1929 petitioner had net taxable income of $56.72; for 1930, a loss of $22,894.68 and for 1931, a net taxable income of $6305.00 (R. 180, 186, 190.) most of the cost of securities in excess of the $584,312.24 shown above was paid by the original cash capital of petitioner rather than from any accumulation of earned surplus. During all the taxable years involved the market value of the securities held was less than cost by considerable amounts. (Supra.)

During the taxable years no dividends were paid and no salaries were paid the officers of petitioner. (Special finding on issue V, R. 61.) Petitioner did not declare dividends during the taxable years involved because it was believed that the earnings were not sufficient to warrant dividends, an increase of assets was desired for future business purposes, and the

value of the assets was impaired. (Testimony, R. 101.) Such failure to declare dividends had very little effect upon the individual income taxes of the two stockholders. The failure to declare dividends did not result from any discussion between the stockholders of possible taxes falling upon either one of them individually. (Testimony, R. 102.) The findings on the income taxes payable by the two stockholders for the three taxable years involved would indicate that such a discussion was entirely pointless because W. T. Wilson paid only $150.00 income tax in 1932 and none in the years 1933 and 1934 while F. A. Wilson paid no tax in any of the years. (Special findings on issue V, R. 59.)

The Board's findings comment on the differences between the balance sheets shown on the income tax returns of petitioner for the three years involved and the balance sheets as they would have to be adjusted to accord with the books of account and the facts. (R. 57, 58 and 59.) These books of account were kept and the returns were made by one of the stockholders who confessedly was not a trained bookkeeper or accountant. (Statement of evidence, R. 89, 113.) While the stockholders of petitioner were satisfied with the system of accounting and could determine its financial status therefrom, nevertheless they readily assented to the employment of a highly reputable firm of certified public accountants to clarify their records of accounts and reconcile them with their income tax returns for the taxable years involved for the purposes of presenting petitioner's cause to the Bureau of Internal Revenue and the Board. (Statement of

evidence, R. 115.) It was petitioner, not respondent, who pointed out the defects in the returns and the books of account. (Statement of the evidence R. 88 *et seq.,* Exhibits 3, 4, 5, 6, 7, 8, 9, 10, 11, 18, 19, 20, 21, 22 and 23.) What was disclosed to the Board by petitioner was a primitive way of keeping accounts, which could be and was, analysed to show the real status of petitioner's affairs and an egotistical but tax harmless method of enlarging capital or surplus by personal I. O. U.'s which meant nothing to anybody but the stockholders.

In its report or memorandum opinion the Board accepts on the testimony introduced by petitioner, not by respondent, the adjustments on the books of account and returns. (Special findings on issue V, R. 57 et seq; Special findings on issue II, R. 35.) On the other hand it rejects certain items proven by the testimony and supported by exhibits admitted in evidence. Furthermore, in its endeavor to sustain the Commissioner on its issue V and thus determine petitioner liable for a surtax for accumulation of surplus, the report or memorandum opinion "assumes" as facts certain things which do not appear in evidence and which, if important, should have been inquired into on cross-examination by respondent. (R. 66.)

In order to present to the Court the essentials of petitioner's financial status for the years in dispute it is necessary to deal with its balance sheets.

Those balance sheets for the years in dispute, corrected to accord with the memorandum findings of fact and opinion of the Board, are as follows:

Assets:	1932	1933	1934	
Cash	$ 96,638.23	$ 9,186.43	$ 73,707.36	R. 58
Notes Receivable	14,000.00	—	—	R. 172
Call Loans	100,000.00	151,000.00	171,000.00	R. 171
Accounts Receivable, Trade	72,662.47	94,924.01	103,002.60	R. 37, 40, 176-178
Accounts Receivable, F. A. Wilson	—	43,234.37	35,612.50	R. 178, 179, 60
Accounts Receivable, W. Wilson	17,717.18	16,917.88	16,917.88	R. 60
Accounts Receivable, Mary H. Wilson	21,248.51	21,128.51	21,128.51	R. 173
Merchandise	—	6,500.00	3,946.60	R. 171
Bonds (cost)	13,425.00	13,445.00	30,245.00	R. 40, 170
Stocks	750,943.50	782,190.55	837,778.05	R. 58, 167-169
Land	30,000.00	30,000.00	30,000.00	R. 181
"Oregon", net after depreciation	90,126.99	83,869.35	77,251.71	R. 52
"Idaho", net after depreciation	48,968.89	45,471.11	41,943.33	R. 51
Furniture & Fixtures, net	1,782.18	1,584.16	1,386.14	R. 53
Autos, net after depreciation	2,436.84	1,263.18	524.52	R. 25
Total Assets	$1,259,950.49	$1,299,715.35	$1,449,972.20	
Liabilities:				
Accounts Payable	$ 3,064.68	$ 2,778.71	$ 3,246.39	R. 171
Capital	1,000.00	1,000.00	1,000.00	R. 57, 58
Earned Surplus (1931—$12,792.64)	19,426.64	47,875.92	86,838.71	R. 68, 231, 171, 71
Capital Surplus	1,236,459.17	1,248,060.72	1,358,789.10	
Total Liabilities	$1,259,950.49	$1,299,715.35	$1,449,972.20	

In the foregoing balance sheet assets and earned surplus are inclusive of the amount of bad debt deductions claimed by petitioner but disallowed by the Board. Similarly, depreciable assets appear at the figures determined by the Board. If petitioner's contentions are sustained, some fairly substantial adjustments will be required for:

Accounts receivable	(Woodhead, "Svea")
Bonds	(Kentucky Fuel Gas)
"Idaho"	(Basis and depreciation)
Earned Surplus	(Partial bad debts, Svea Account, additional depreciation, income tax liability accrued)

Some adjustment will also be required for "capital surplus".

The actualities of earned surplus accumulations are of the greatest significance, because without considerable accumulations no purpose to avoid surtax can be found. The petitioner's earned surplus as found by the Board and the adjustments thereto contended for by petitioner for the purpose of determining petitioner's accumulations are as follows:

	1931	1932	1933	1934
Surplus per B. T. A.	$12,792.64	$19,426.64	$47,875.92	$86,838.71
Woodhead, partial bad debt				5,000.00
Kentucky Fuel Gas, do.				5,500.00
"Svea"—expenditures not an asset	6,420.36	9,081.78	10,804.01	12,861.01
Add'l depr. Idaho		2,600.00	5,200.00	7,800.00
Surplus adjusted	$ 6,372.28	$ 7,744.86	$31,871.91	$55,677.70

Any corporate director of ordinary intelligence, in determining the amount of earned surplus available for distribution as dividends would consider carefully the market value of the more important assets. The charges made against the Woodhead Lumber Co. of California and the Kentucky Fuel Gas Bond accounts in 1934 were actually insufficient to reduce those accounts to their true worth. An expert witness, testifying for petitioner, stated that irrespective of the deductibility of the charge off on the Kentucky Fuel Gas Bonds, their asset value should be written down by at least $5500.00 for purposes of corporate financial statements. (R. 128.)

Certainly the same observation is true of the $42,000.00 account receivable of the Woodhead Lumber Co. of California, a corporation out of business and with assets of a maximum value of $25,000.00. By the end of 1934 this account should have appeared at not more than such maximum, with a further reduction in earned surplus of more than $12,000.00.

The "account receivable" resulting from the petitioner's expenditures for maintenance of the "Svea", as managing, disbursing, and collecting agent, was never an asset. The Board, in discussing the deductibility of the write offs against this account finds only a moral obligation to repay petitioner for these expenditures, and that petitioner was not a creditor as to them. (R. 39, 40.)

The Board committed grevious error in considering these accounts only with respect to the deductibility of the charges made against them, and in failing to

consider them with respect to the question of petitioner's accumulation of surplus. In fact, the Board wholly failed to determine in the memorandum findings of fact and opinion what surplus petitioner had accumulated!

In addition to the reductions of earned surplus hereinabove discussed, further reduction should be made for other impaired assets. The steamers "Oregon" and "Idaho", while having a very substantial cost basis, had not been in operation for several years because they could not be operated at a profit. (R. 35, 36.) During the years in question they necessitated large expenditures for maintenance and repairs. If petitioner could not profitably operate those steamers in its own business, their value to anyone would be very speculative and very small.

Thus, in realistic sense, petitioner, during the years in question, never had or accumulated any earned surplus whatever.

The respondent's determination on this issue for 1934 is in the following language:

> "An examination of the balance sheets submitted with the return leads the Bureau to conclude that your corporation is an investment corporation and subject to the provisions of Section 102 of the Revenue Act of 1934." (R. 18.)

In the deficiency notice for 1932 and 1933 respondent stated: "after careful consideration of your Federal income tax returns and of all other available evidence the Bureau holds that your corporation is subject to taxation under the provisions of Section

104 of the Revenue Act of 1932 for the years 1932 and 1933."

The balance sheets upon which respondent's determination was based were erroneous, principally in their treatment of shareholders' I. O. U.'s as being the equivalent of cash. No specific reason is stated for respondent's determination for 1932 and 1933, but apparently after examining the balance sheets contained in the returns he concluded, as he did for 1934, that petitioner was a mere holding or investment corporation.

While petitioner had large investments, it was not an investment corporation. It was organized for a particular purpose, i.e., logging, manufacture of lumber, and the purchase, sale, and transportation of lumber and the operation of steamships. (R. 56.) While the realization of that purpose was delayed by a worldwide depression, every act and omission of petitioner is consistent with that purpose.

A very large capital would be required. Petitioner's two shareholders undertook to supply it by equal contributions and by the preservation of the corporate assets. Their failure to declare dividends or pay salaries to themselves, particularly in the face of the impairment in value of many of the corporate assets is consistent with that purpose. The corrected balance sheets show some capital contributions during the taxable years. Apparently the respondent and the Board would require petitioner to declare and pay dividends to the shareholders at the same time they were making capital contributions to petitioner for its business purposes.

Both the respondent and the Board ignored the business purpose of the petitioner. The Board determined that petitioner was FORMED for that business purpose. (R. 60.) It then holds that was AVAILED OF for the prohibited purpose of avoiding surtax on its shareholders. The Board does not find that the purpose for which petitioner was organized was ever abandoned; it could not so find in the face of the positive and uncontradicted evidence to the contrary. (R. 101.) The fulfilment of that purpose was postponed for business reasons—the fact that lumber and shipping concerns were operating at a loss—but it was never abandoned. (R. 101-102.)

In discussing and allowing petitioner's expenditures for the maintenance of the "Idaho" and the "Svea" the Board said (R. 35, 36):

> "The steamers were acquired by petitioner in January, 1929 principally for the purpose of transporting lumber. After acquisition they were operated only five or six months before they were 'laid up', because business got so bad that they could not be operated at a profit. The country was then experiencing a depression which lasted several years. During the taxable years the steamers were kept in a seaworthy condition, in order that petitioner might use them if opportunity was afforded to profitably resume lumber transportation. The ships were never abandoned, but were always in charge of some one to look after them. The ships were put in dry dock and their bottoms were painted to protect and preserve them. Watchmen were employed and paid to look after them and certain supplies were furnished. Repairs were made to maintain the ships in proper

> serviceable condition. Petitioner always expected to put the ships back into commission and re-engage in the shipping of lumber when conditions became favorable * * *''

These same facts are most material to the surtax issue but receive but little mention by the Board in its finding and opinion relating thereto. The Board does find that the corporation "always had the purpose of engaging in the lumber and shipping business", that the partnership's capital in such business had been $1,500,000.00 and that at the date of the hearing at least as large an amount would be required. (R. 56, 63.)

In sustaining the respondent on this issue the Board's opinion may be said to consist of the following arguments:

(1) "Because the testimony of the capital required by petitioner for full and complete logging, lumber manufacturing, and shipping business did not relate specifically to the taxable years, no business reason was shown for the accumulation of its comparatively small surplus." (R. 63, 64.)

(2) "The positive and uncontradicted testimony of W. T. Wilson would defeat the imposition of the tax if believed. It is discredited, however, by the false balance sheets annexed to the returns, which returns were over the oath of the same witness." (R. 62, 63, 66.)

(3) "The corporation did but little business during the taxable years, and did not re-engage in logging, lumber manufacturing, and shipping because those

businesses were losing money—these statements almost put petitioner out of business." (R. 64.)

(4) "F. A. Wilson and W. Wilson (whom we can assume to be W. T. Wilson) were permitted to owe petitioner on accounts receivable. They therefore treated petitioner pretty much as they pleased." (R. 65, 66.)

(5) "The two shareholders of petitioner paid no income tax during the years in question, except for about $150.00 paid by W. T. Wilson for 1932. Hence they gained a substantial tax advantage by petitioner's failure to pay dividends." (R. 59, 66.)

The foregoing points made by the Board will be discussed in the order in which they appear above.

(1) The Board's argument with respect to the absence of proof of a reasonable business need for the accumulation of petitioner's small earned surplus is self-defeative. While it is true that petitioner's actual business was small and required little capital, its contemplated operations were extensive and would require a great deal. The actual amount required could not possibly be accurately known in 1932, 1933 and 1934 because the petitioner did not, in each of those years, contemplate immediate enlargement of its business.

Petitioner contemplated the enlargement of its business as soon as a reasonable demonstration of probable profits indicated it could profitably do so. Naturally the culmination of that purpose would be postponed for as long as other logging, lumber manufacturing and shipping concerns were losing money. Petitioner's

business purpose would be defeated if its assets were invested in a losing enterprise. It was promoted by investments in liquid income-paying assets. While petitioner could unquestionably purchase timberlands for less when those lands could not be profitably logged, it naturally preferred to wait and pay more later when it had a reasonable assurance of profits.

Evidence of the cost of full scale operations during the taxable years in question is absolutely immaterial to the issue. They were all depression years and while timberland *speculation* during them might be justified, *business investment* could not.

The business need for the accumulation was the greater because of these facts. Petitioner could not and did not know how much ready capital it would need as conditions improved and prices rose. It wanted to have enough to meet that need, whatever it might be. Therefore, it paid neither salaries nor dividends to its officer-shareholders.

The Board's argument is interesting on this phase of the issue. As heretofore stated, it would take a prescience beyond that of petitioner's officers to accurately estimate its cash (or equivalent) needs. Yet the Board of Tax Appeals can say "you have more than you need (needed); our judgment is superior to yours when it comes to an estimate of your needs".

The Board's determination on this phase of the issue is directly contrary to two cases in which it was held that the prospective needs of the future contemplated enlarged activities were the governing consideration. As long as the intention to enlarge opera-

tions continued to be the reason for accumulation of surplus, the surtax asserted was improper.

William C. De Mille Productions, Inc., 30 B. T. A. 827, 830;

Cecil B. De Mille, et al., 31 B. T. A. 1161, 1175, aff'd 90 F. (2d) 14.

The facts in the last cited case are similar but much less favorable to the taxpayer. The taxpayer's income was from contracts for personal services, its surplus as high as $1,606,575.33.

(2) Admittedly the balance sheets were inaccurate from the standpoint of an expert accountant. W. T. Wilson was not an expert accountant and made errors inconceivable to an expert. The greatest errors were in treating the I.O.U.'s of himself and his brother as the equivalent of cash and in treating capital surplus as capital. The other errors followed almost inevitably from these two, with the further factor that the two brothers were the sole shareholders, officers and directors of petitioner and understandably omitted formal corporate procedure. Thus when they agreed that the corporation should have treasury stock, they failed to actually transfer shares to it. As far as they were concerned, they understood the act as the same as if actually accomplished. No one was injured by this procedure. There were virtually no creditors. The Federal Government was not prejudiced in any way. The gross income of the corporation was correctly stated, and except for the disputable items of partial bad debts and depreciation allowance, so were the deductions.

Regardless of how inexcusable are the errors in the balance sheets, they illustrate no desire to defeat or defraud either the Federal Government or anyone else. It has been shown (*supra*) that it was the petitioner who undertook to supply the respondent and the Board with accurate balance sheets. The only effect of the errors contained in the returned balance sheets was to lead respondent to believe that a surtax was due (R. 18, 222), and therefore make a determination which otherwise would probably not have been made.

These facts do not excuse the Board in treating the direct, positive, and otherwise unchallenged testimony of W. T. Wilson as the equivalent of perjury, or believing it in part and discarding it in the parts disadvantageous to the conclusions sought to be reached.

(3) While petitioner's active business transactions were limited and not particularly profitable, it must be remembered that the years in question were the years of severest depression. Petitioner was doing the best it could and all it could to maintain a going business in the face of adverse circumstances. The Court will take judicial notice that like conditions existed with like and other lines of business throughout the country.

The Board member was obviously guilty of an error of law when he considered the surplus accumulations in the light of actual business operations rather than in the light of contemplated business operations and needs. *Cecil B. De Mille, et al., supra.*

The member's conclusion that the witness' statements almost put the petitioner out of business is

hardly worthy of comment. The witness testified that logging, lumber manufacturing, and shipping businesses were losing money during the years 1932-1934, and that, therefore, petitioner did not engage in any of those enterprises. (R. 64.) This testimony related to petitioner's delay in fulfilling its business purpose to the complete limit of that purpose. It had nothing to do with petitioner's wholesale lumber business.

Petitioner's lumber business was increasing during the years in question, as shown in the following table:

	1929	1930	1931	1932	1933	1934
Sales	$353,833.46	$139,196.14	$64,571.55	$28,725.96	$92,862.09	$170,239.51
Gross Profit on sales	47,757.63 (R. 180)	11,914.14 (R. 186)	(5,151.15) (R. 190)	(4,629.77) (R. 132)	8,424.60 (R. 142)	20,152.56 (R. 153)

The Board member in stating that petitioner had no immediate need in 1932-1934 for the small surplus accumulated may be even logical from the viewpoint of 1940, when he considered the proceedings. How immediate the need *seemed* to petitioner's officers at any time during 1932, 1933 and 1934 is another question. And of course, because the surtax can be found only where the intent was to accumulate, not for business reasons, but for avoidance of tax by the shareholders, our inquiry must be to things as they seemed.

Petitioner's business in 1933 was better than it had been in 1932. It was better yet in 1934. With this improvement naturally the time for full-fledged operations in accordance with petitioner's purpose seemed more imminent.

The Board apparently considered the smallness of business done by petitioner and the absence of large profits therefrom to have been the result of deliberate self-sabotage. It apparently chose to ignore the self-interest of petitioner in making profits, and also, at this point, the universally known facts concerning the depression.

(4) The Board seemed to place great emphasis and reliance on the fact that F. A. Wilson and W. Wilson (assumed by the Board, without a shred of evidence to support its conclusion, to be W. T. Wilson) were permitted to owe the petitioner on accounts receivable. From this fact and assumption it concluded that the shareholders treated petitioner pretty much as they saw fit. (R. 65.)

The record proves the contrary. In the first place, these accounts receivable were being reduced at the same time each of petitioner's shareholders were making contributions to petitioner's capital! They were not borrowing sums from the corporation.

In the second place, the detailed analysis of the account of F. A. Wilson discloses the account to be the result of stock brokerage transactions undertaken by him for the benefit of the corporation, in reality a trust relationship rather than a debtor-creditor relationship. This account was closed by petitioner's payment to F. A. Wilson of $37,366.25 in December of 1934 and his delivery to petitioner of Kennecott Copper Co. and other shares costing $35,612.50 on January 2, 1935. He wasn't dealing with the corporation, he was acting for it. (R. 178, 179.)

In the third place, upon what basis does the Board assume "W. Wilson" to be W. T. Wilson? There is no evidence or testimony upon which such an assumption could properly be made.

The Board felt that the picture of the accounts receivable was similar to that presented in *Rands, Inc.,* 34 B. T. A. 1094. (R. 66.) Petitioner fails to see the similarity.

In the *Rands* case, *supra,* the corporation was organized by the principal shareholder with the conveyance to it of $1,502,273.17 in stocks and bonds. It was formed as a speculative medium for dealing in stocks, bonds and real estate. One shareholder held over 99 per cent of the stock of the tax payer and alone guided its policy. The tax payer's principal activities consisted of *trading* in common stocks of a speculative nature, amounting to between 100 and 160 transactions per day. The principal shareholder *lent* sums running to nearly $2,000,000.00 to the tax payer for stock speculations. His remaining assets consisted largely of tax exempt bonds. The tax deficiencies involved (principally the 50% surtax) amounted to $315,306.91 for 1927, $475,025.87 for 1928, $239,051.62 for 1929, and $28,614.83 for 1930, indicating average earnings of more than $500,000.00 per year, none of which were distributed.

On the other hand, this petitioner was formed for a business purpose and this purpose was never abandoned. The years in question were depression rather than "boom" years. Petitioner's two shareholders lent none of their funds to petitioner. It does not

appear that any of their holdings were tax exempt and because of respondent's failure to offer evidence on that point we may safely assume they were not tax exempt. If petitioner had currently distributed all of its very small earnings each year little or no tax would have had to be paid by the shareholders. Petitioner's earnings never exceeded 3 per cent of its capital. The annual earnings of Rands, Inc. amounted to as much as 50 per cent of its capital. Petitioner's shareholders had no transactions with it during the years in question; Rand's principal shareholder had many.

Where is the similarity? There is none whatever. *Rand's Inc., supra,* rather than supporting the Board, indicates the arbitrariness and unreasonableness of the Board's opinion on this issue.

Furthermore, in the *Rand's* case, *supra,* and in all other cases in which the imposition of the surtax has been sustained, no business purpose was shown for the acquisition of stocks and bonds. Here the business purpose was shown and was found to exist during the taxable years. The Board accedes to the purpose but substitutes its own judgment as to the reasonableness of the need.

The contributions of petition's shareholders to it were of cash rather than of stocks and bonds. There is therefore no implication in the record that if petitioner had never been created their income would be any greater than it was after petitioner's creation. The larger transfers to petitioner, at least, were of cash lying idle in bank, and were not the result of

sales by the shareholders. (R. 90, 109.) Can it be assumed that in the absence of the transfers to petitioner its shareholders would have invested this cash? They had not done so prior to the transfers.

(5) The Board apparently felt that the fact petitioner's shareholders (with the single exception of W. T. Wilson for 1932) paid no income tax whatever was proof that petitioner was availed of for the prohibited purposes. Petitioner believes that this fact is positive and incontrovertible proof of the contrary. Unless tax was in fact avoided, the prohibited intention cannot be found.

It is significant that the originals of the returns of petitioner's shareholders were in respondent's possession, but were not placed in evidence in this proceeding. It may well be that those returns would show, with the single exception above noted, that if *all* the earnings of petitioner had been currently distributed, no increase in tax would have resulted.

Even in the absence of its business purpose it would not be reasonable to require petitioner to distribute the last cent of its annual earnings and profits. Some of petitioner's assets and particularly the steamships, the Kentucky Fuel Gas Bonds, the accounts receivable from Woodhead, and the account represented by expenditures on the Svea, were of a value far less than that carried on the books. If these items had been written down to their true worth, petitioner would have no earned surplus to distribute in any of the tax years involved, which same years presented a very doubtful and uncertain picture for the future.

The net earnings of petitioner for the year 1932 were less than $7000.00, as found by the Board. And the Board found that as to the $6420.36 item of Svea advances, petitioner was not a creditor; it was only a moral obligation. (R. 38, 39.)

The taxes determined in this proceeding are $3316.84 for 1932, $11,652.75 for 1933, and $15,724.73 for 1934. The original deficiencies asserted were much larger. (R. 69, 31.)

Even assuming that the entire earnings for 1932 as found by the Board were distributed pro-rata to the shareholders, each would have to report a dividend of $3317.00. F. A. Wilson's tax on this might be nothing and *could not possibly exceed $33.17.* W. T. Wilson's additional tax *could not possibly exceed $375.36.* These figures assume the respective shareholders to have other net income subject to surtax (and in excess of their allowable credits) of $6000.00 and $18,250.00, respectively.

Revenue Act of 1932, Section 12(a).

If petitioner had distributed *all* of its earnings for 1933 as found by the Board ($28,449.28), *the maximum possible tax liability* of each would have been $479.94 on a surtax net income of $20,449.28.

Revenue Act of 1933, Section 12(a).

If petitioner had distributed *all* of its earnings for 1934 as found by the Board ($38,962.79) *the maximum possible tax liability* of each would have been $1813.83 on a surtax net income of $23,481.40.

Revenue Act of 1934, Section 12(b).

All the figures above-given of possible maximum tax liability assume sufficient other income to exhaust all deductions, exemptions and credits and yet leave surtax net income up to the point of commencement of surtax liability.

It would be just as reasonable to assume, during these depression years, that the shareholders had bad debts and other deductions which would eliminate any additional tax from complete distribution of petitioner's earnings.

The Board's determination, as hereinbefore stated, was not based upon any adjusted figures of petitioner's earned surplus. It was apparently based, as was the Commissioner's determination, upon the figures set forth in the deficiency notice. (R. 55.) A comparison of these figures with those as corrected to accord with the Board's opinion will show that the essential premise of accumulations of surplus was greatly exaggerated.

	1932	1933	1934	
Annual Earnings per respondent	$21,731.50	$38,415.51	$44,071.25	(R. 55)
As corrected for decision	6,634.00	28,449.28	38,962.79	
Difference	$15,097.50	$ 9,966.23	$ 5,108.46	

The respondent's determination was clearly predicated on errors, and the Board never took these errors into consideration. Petitioner believes that in the argument on the preceding issues additional errors have been established, the effect of which is to further destroy one of the essentials which must exist

in order for petitioner to be held liable for the surtax. The effect of these errors must be taken into consideration, and if necessary, the case should be remanded to the Board to consider their effect.

It is one thing for the Commissioner and Board to say the accumulation of $22,000.00. of earnings in 1932 exhibits the prohibited purpose. That is bad enough. But it is far worse when the determination based upon $22,000.00 is sustained without discussion or consideration that the $22,000.00 never existed and was an exaggeration of 300 per cent!

The Board should have determined, *prior to making its determination on this surtax issue,* just exactly what petitioner's accumulations were. It should then have determined how much of those small accumulations, if any, were available for and should have been distributed currently as dividends. It should finally have considered the effect upon the shareholders' tax liability of the distribution of such dividends.

The Board actually did none of these things. If it had done them it would have discovered that little or no tax liability was saved petitioner's shareholders. It would then have been forced to believe W. T. Wilson when he testified that dividends were not declared because the assets were impaired; because a large liquid capital was desired with which to engage, as had a predecessor partnership with a capital of $1,500,000.00, invested in logging, timber lands and lumber mills, and engaged in operating steamers. It would have been forced to believe that witness

when he testified that the failure to pay dividends was not the result of any discussion between the shareholders of possible taxes on either of them. (R. 101-103.)

The foregoing testimony was positive and unequivocal. It was not made the subject of any cross-examination nor contradicted by any other evidence. It is a part and parcel of all of the evidence and is in accord with it, and was disbelieved solely because petitioner's balance sheets contained errors immaterial to any issue in this or any other proceeding. It is directly supported by the evidence and findings of petitioner's business purpose, the transfers made to petitioner every year pursuant to that purpose, and the absence of any material increase in the shareholders' tax liability had petitioner never been created or had petitioner currently distributed all its earnings.

Petitioner submits that the surtax liability determined against it was improper and is not supported by any evidence. The Commissioner erroneously determined an excessive amount of earnings for each year. The Board failed to correct the Commissioner's errors. Certain amounts of petitioner's earnings are still in dispute. It had a legitimate business reason for accumulating all the liquid assets it could acquire and its shareholders, by transfers to capital surplus, were aiding that purpose. It was not, as erroneously found by the Board, being dealt with by its shareholders as they pleased. Neither of them borrowed from nor loaned to it in the taxable years. F. A. Wilson dealt for petitioner as a stock broker, and not with

it. Because of small earnings, impaired assets, and its business purpose petitioner paid no dividends. Its failure to pay dividends was not because of any discussion between or purpose of its shareholders to avoid tax on their individual incomes. Little, if any, additional tax would have been paid by those shareholders if the petitioner had currently distributed all of its income as found by the Board. The Board's determination of income was excessive. Petitioner had no net earnings available for dividends.

Petitioner submits that on this issue the Board of Tax Appeals should be reversed. At the very least, and in fairness to petitioner, the cause should be remanded to the Board to reconsider this issue in the light of petitioner's earnings of each year as corrected by this Court, its earnings available for dividends, and the effect of the payment of dividends on both the corporation, in the light of its business purpose, and upon the shareholders, in the light of their individual tax liability for the years in question.

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5. THE BOARD ERRED IN FINDING AND DETERMINING FOR EACH OF THE TAXABLE YEARS INVOLVED THAT PETITIONER WAS LIABLE FOR A FIVE PER CENTUM NEGLIGENCE PENALTY.

In his deficiency notices upon which the two proceedings were initiated before the Board of Tax Appeals the Commissioner states as his reason for the determination of the negligence penalty for each of the taxable years involved as follows:

> "The understatement of tax * * * is attributable to negligence." (R. 19, 224.)

This statement contains the only issue petitioner was required to meet and the only ground upon which the Board can have jurisdiction, to determine a negligence penalty under such deficiency notices. Had there been an intentional disregard of rules and regulations the Board could not consider it, because the Commissioner did not determine the alternative ground provided in section 293(a), *post,* as a basis for the penalty, nor plead it in his answers. For anything beyond his assertions in the deficiency notices the burden was on the Commissioner to plead and prove. As to facts, we again have an example of the Board's isolation of specific findings from general findings. The Board makes no findings in this issue VI, but states: "The facts above set forth and reviewed in discussion of section 104" (Issue V in the report or memorandum opinion and part 4 of this brief) "are here applicable with equal force." The purpose and terms of section 104 are so far apart from the provisions of the statute here to be considered that we cannot conceive how the Board could for one moment consider the facts under one statutory provision to be "applicable with equal force" to an entirely different provision. Moreover, the facts on issue V do not apply to issue VI.

To clarify this assertion, we quote the material part of section 293 of the Revenue Act of 1932, which is identical in language with section 293 of the Revenue Act of 1934, viz:

> "SEC. 293. ADDITIONS TO THE TAX IN CASE OF DEFICIENCY.

(a) *Negligence.* If any part of any deficiency is due to negligence, or intentional disregard of rules and regulations but without intent to defraud, 5 per centum of the total amount of the deficiency (in addition to such deficiency) shall be assessed, collected, and paid in the same manner as if it were a deficiency * * *''

(N. B.) By its punctuation the above section clearly makes ''negligence'' something apart from ''intentional disregard of rules and regulations.'')

The Commissioner in his application of the above quoted section asserted that the penalty for each year was added to the deficiency because ''the understatement of tax'' * * * ''is attributable to negligence'' (R. 19, 224.) but he did not refer to ''rules and regulations'' nor define what acts or omissions constituted the negligence upon which he imposed the penalty by any explanation in the deficiency notices; nor did he plead affirmative allegations in his answers which enlarged the reasons set forth in the deficiency notices or in any way referred to ''disregard of rules and regulations.'' (R. 19, 227.) We are therefore left with but one cause for the assertion of the penalty, viz: the returns failed to report income or sought deductions which reasonable judgment did not warrant. No matter how poorly the books of account of petitioner may have been kept, and such fact seems to be the basis of the Board's decisions, let us look for ''the understatement of the tax'' in the returns which, as far as the record shows was, in the Commissioner's mind when he asserted negligence. The

section quoted above deals only with negligence in reporting income, not in keeping books and records.

(1) Gross Income as reported for normal tax in the returns for petitioner (Exhibits 3, 4, and 5) was: $32,565.57 for 1932; $75,579.28 for 1933; and $63,-901.60 for 1934. The only challenge the Commissioner made to gross income as returned was to add interest to that income for the years 1932 and 1933. These additions were disallowed by the Board in issue I of its report or memorandum opinion. (R. 33-35.) Certainly there was no negligence on the part of petitioner in reporting gross income.

(2) Deductions sought by petitioner in its returns for the three years involved constitute the main grounds for dispute between the parties in relation to the net taxable income for normal tax. (R. 32.)

(a) For maintenance of steamships petitioner's returns claimed $4547.05 for 1932; $4412.26 for 1933; and $2173.18 for 1934. The Commissioner allowed the deduction for 1934 and the Board sustained petitioner's claims for 1932 and 1933 in issue II of its report or memorandum opinion. (R. 35-37.) Where was the negligence on this point?

(b) Partially bad debts written off consist of three items, viz.: on accounts receivable from Woodhead Lumber Co. of California in the amount of $5000.00 for 1934; accounts receivable from "S. S. Svea" in the amounts of $2160.80 for the year 1933 and $4644.40 for the year 1934; and accounts receivable on bonds of the Kentucky Fuel Gas Corporation

in the amount of $5500.00 for the year 1934. While the Board has determined adversely to the petitioner on these claimed deductions, it has not done so on the grounds of any negligence on the part of petitioner, excepting, perhaps, in failure of proof on hearing to which section 293, *supra,* would not apply. On the other hand petitioner has appealed to this Court from the Board's determinations of non-deductibility of the partial write-offs and deductions relating to the accounts of the Woodhead Lumber Co. of California and Kentucky Fuel Gas Corporation bonds under the firm belief that the determination of the Board was erroneous. As argued under Point No. 1 *supra,* the determination of a partial write-off is a matter of judgment and if this Court seeks to sustain the Board in disallowing these claimed deductions it cannot determine that an error in judgment is negligence. With regard to the deductions sought on the accounts receivable from the "S. S. Svea", while we do not appeal from the decision of the Board, it may be said that there were advised errors in judgment under circumstances which in no way may be attributed to negligence. The fact that the Board finds that the accounts receivable amounted to $9081.78 on January 1, 1933, and to $10,-804.01 on January 1, 1934; that there was a moral obligation on the petitioner to keep the vessel in repair, and that it was advised by an attorney that "it did not look like recovery could be made and a suit would be foolish" (R. 39) would naturally lead petitioner to seek partial deductions. If there was a failure of proof before the Board, as found (R. 40), such failure on hearing before the Board cannot constitute

negligence in making the returns and the Board in denying the deduction does not so find. (R. 38-40.)

(c) Depreciation constitutes the next items of deductions sought and, for each of the years, as per the returns, was as follows:

	1932	1933	1934
Wooden buildings	$1,000.00	$1,000.00	$ 500.00
Automobiles	900.00	1,649.85	1,649.85
S.S. Idaho and Oregon	8,750.00	8,750.00	8,750.00
Furniture and fixtures	500.00	500.00	500.00

The parties stipulated the depreciation allowances on the wooden buildings and automobiles before the proceeedings came before the Board. (R. 33.) Therefore, those items were not before the Board for consideration in any way and it was not called upon to pass judgement on the claims of petitioner or the adjustment with respondent in any way. With regard to the steamships we would point out that after the returns for the three years had been filed, the Commissioner extended the depreciable life of the vessels by fifteen years and changed the theretofore accepted rate of depreciation. (R. 46, 225.) He also decreased the residual value of the vessels which petitioner contested and, as to "S. S. Idaho", is contesting in these cases. These factors could not have been considered by petitioner in making its returns. However, on the determination of the amount of depreciation made by the Board and its decision made upon the computation of respondent, $9935.42, or $1185.42 in excess of the amount claimed by petitioner in its returns, was decided to be the amount which petitioner was entitled to deduct as depreciation on the two vessels. If there

was negligence here, it certainly was not such as should subject petitioner to a penalty. With regard to depreciation on furniture and fixtures the petitioner took the same deduction for 1929, 1930, and 1931 as it did for the three years involved and such deductions were allowed for the first three years by respondent. (R. 52.) Can it be said that petitioner was negligent in 1932, 1933 and 1934 for what the Commissioner allowed for the first three years of the petitioner's life? We do not think so. Long after the deductions of the first three years had been followed for the next three years (R. 220, 225) the Commissioner changed the cost basis and increased the depreciable life of the furniture and fixtures, thereby reducing the annual rate of depreciation. In contesting this action before the Board, the Commissioner's acts were approved, but on account of petitioner's failure to sustain the burden of proof of cost at the hearing and not on the ground of negligence in making the returns. (R. 53, 54.)

We have covered all of the items which affect the net income of petitioner for normal tax for the three years involved and can discover no "understatement of tax * * * attributable to negligence" as claimed by the Commissioner. The poor bookkeeping methods and the I. O. U.'s upon which the report or memorandum opinion dilates have nothing to do with the penalty for negligence which the Commissioner contemplates in his assertion of reasons for imposing one. When we compare the Commissioner's enlargement of income in his deficiency notices for normal tax purposes with petitioner's returned income for each of the years and

with the income determined by the Board, we find the greater error on his part. Was he negligent?

	1932	1933	1934
Normal tax returned by petitioner	None	None	None
Normal tax determined by Commissioner	$11,343.36	$22,078.01	$2,614.46
Normal tax determined by Board	None	1,499.93	1,912.05

We believe that these figures show that there were matters involving controversy between the parties but that, when the Commissioner so woefully fails to sustain his enlargement of the tax he cannot under the reasons alleged by him claim penalty against petitioner, and the Board erred in sustaining even a fragment of his asserted penalty.

(d) A penalty for negligence for failing to return a surtax is something difficult to comprehend, because a taxpayer who reasons that he should not dividend his surplus and forms his judgment and makes his return on that basis must deny his reasons and deem his judgment poor if he does return and pay surtax. The Board found and this Court may take judicial notice of the fact that during the taxable years the nation was in such a state of depression and economic panic that no one could tell what the morrow would bring. There was no negligence as far as the books of account or the returns are concerned in setting forth the items which might render petitioner liable for surtax. The income from all sources was accurately reported in the returns. We believe that we have shown in our argument on the immediately preceding issue that the surplus accumulated was not adequate to require a return for surtax. But, if this court should determine to the contrary, there is no negligence such

as the Commissioner contemplated to warrant the imposition of a five percentum penalty. More important is the fact that there is no place on a corporation return to report surtax, nor any provision in any law requiring the reporting of surtax liabilities.

We ask the Court to read the short opinion on issue VI (R. 67) to see what fallacious reasoning is used to determine the penalty. The negligence asserted by the Commissioner relates to "understatement of the tax", not to enlargement of cash through I. O. U.'s, erroneous treatment of capital stock, or maintaining no cash book. The things which the Commissioner claimed as a result of these things, with the exception of the surtax, were entirely demolished by the Board's findings and decision, as shown by the comparative tabulation above. Yet the Board says: "Obviously, a part of the deficiency was due to 'negligence or intentional disregard of rules and regulations' without which the tax in this case could have been ascertained without all the difficulty encountered". What "part of the deficiency was due to negligence" the Board does not find. "Obviously" the deficiencies were made more difficult to ascertain through the unwarranted acts of the Commissioner than they were by any acts of petitioner as is clearly disclosed by the tabulation of normal tax shown above. "Obviously", other than in the dogmatic statements contained in issue IV of the report or memorandum opinion, there is no finding that there was any negligence on the part of petitioner, and certainly no specific findings of fact upon which the opinion could be based. Incompetence or ignorance do not constitute negligence.

As we have pointed out, the adjustment of normal income which produced the deficiencies found by the Board resulted entirely from adjustments of deductions sought by petitioner in its returns. As we have shown in the foregoing argument there was reasonable ground for petitioner to claim all its deductions and to differ from the conclusions reached by the respondent. Under such circumstances no negligence penalty should be allowed.

Herman Senner v. Commissioner, 22 B. T. A. 655, 658; Acq. X-2 C. B. 64;

Frank T. Heffelfinger v. Commissioner, 32 B. T. A. 1232, 1234;

Davis Regulator Co. v. Commissioner, 36 B. T. A. 437, 444; Acq., 1937-2 C. B. 7.

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6. **THE BOARD ERRED IN NOT MAKING ITS FINDINGS OF FACT COMPREHENSIVE AND GENERAL SO THAT, WHERE MATERIAL, THEY WOULD APPLY TO ALL ISSUES. IT FURTHER ERRED IN SEPARATING AND DIVIDING ITS FINDINGS UNDER SEPARATE ISSUES AND THUS MAKING FACTS APPLICABLE ONLY TO ONE ISSUE AND EXCLUDING SUCH FACTS FROM OTHER ISSUES TO WHICH THEY WERE MATERIAL. IT FURTHER ERRED IN INTERMINGLING FINDINGS OF FACT, CONCLUSIONS OF FACT AND CONCLUSIONS OF LAW SO AS TO RENDER PORTIONS OF ITS DECISIONS ARBITRARY AND ERRONEOUS IN FACT AND LAW. IT ALSO ERRED IN NOT MAKING ITS FINDINGS OF FACT AND CONCLUSIONS OF LAW CONFORM TO THE EVIDENCE.**

Under this heading we have consolidated specifications of error numbered 19 to 24 in the Petitions for Review. (R. 78, 241.) In making these assignments of error, we appreciate that we are doing the unusual.

However, the report or memorandum opinion for the two cases is so unusual as to require special treatment and comment. In no reported case within the knowledge of the writers hereof has a Court or Board by specific direction excluded findings from consideration on all issues to which they might be material and confined their application to a single issue as the Board has done by its declaration:

> "The other issues will be considered in the order above set forth, the facts, except the general facts as to incorporation stated above, being set forth separately in connection with discussion of each issue." (R. 33.)

If facts are to be found issue by issue, then the facts should be found fully as to each issue. This the Board did not do.

This error is particularly noticeable in issue VI of the report or memorandum opinion where no facts applicable to the issue are found. Reference is made to the facts found in issue V, which make no reference to negligence nor any facts applicable to negligence.

As we have pointed out the strange results of the strange separation of findings of fact in our discussion of the prior assignments of error we will not extend this brief by reiteration. We believe we have shown that, by its isolation of facts in finding separately for different issues, the Board has violated the rules laid down for its observance by the Courts.

> "The Board of Tax Appeals, recognizing the fact that its rulings of law are reviewable, should make all reasonably requisite findings of fact."
>
> *Brampton Woolen Co. v. Commissioner,* (CCA 1), 45 Fed. (2d) 327.

VI. PRAYER FOR RELIEF.

WHEREFORE, petitioner prays this Court to hear the proceedings and to reverse the decisions of the United States Board of Tax Appeals on the issues hereinbefore presented, and for such other and further relief as to this Court may seem meet and proper.

Dated, San Francisco,
June 6, 1941.

ADOLPHUS E. GRAUPNER,
LOUIS JANIN,
Counsel for Petitioner.

Nos. 9781 and 9782

In the United States Circuit Court of Appeals for the Ninth Circuit

WILSON BROTHERS & COMPANY (WILSON BROS. & CO.), A CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITIONS FOR REVIEW OF THE DECISIONS OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

SAMUEL O. CLARK, Jr.,
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ARTHUR A. ARMSTRONG,
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OPINION BELOW

The memorandum opinion of the Board of Tax Appeals (R. 31–67) is unreported.

JURISDICTION

The Board entered its decisions on August 6, 1940 (R. 68, 231–232) finding deficiencies as follows:

Year	Normal Income Tax	Additional Tax under Section 104 of the 1932 Act, and Section 102 of the 1934 Act	Penalty
1932	None	$3,316.84	$165.84
1933	$1,499.93	14,224.80	786.24
1934	1,912.05	9,740.70	582.63

The case is brought to this Court by the taxpayer's petitions for review filed October 31, 1940 (R. 69–82, 232–245), pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

QUESTIONS PRESENTED

1. Is there substantial evidence to support the Board's conclusion that the Commissioner was justified (under Section 23 (k) of the Revenue Act of 1934) in refusing to permit deductions for the year 1934 on account of debts alleged to have become partially worthless in that year?

2. Did the Board properly determine the basis for depreciation purposes (under Sections 113 (a) (2), 113 (a) (8), 113 (b), and 114 (a) of the Revenue Acts of 1932 and 1934) of property acquired by taxpayer corporation by gift or acquired by its stockholders by gift and contributed by them to its capital?

3. Is there substantial evidence to support the finding of the Board that in the years 1932 to 1934, inclusive, the taxpayer was availed of to avoid the imposition of surtaxes upon its shareholders and therefore was subject to Section 104 of the 1932 Act and Section 102 of the 1934 Act, providing for additions to normal taxes under such circumstances?

4. Is there substantial evidence to support the finding of the Board that part of the deficiency for each of the years 1932 to 1934, inclusive, was due to negligence and therefore that the deficiencies for those years were subject to penalties as provided for in Section 293 (a) of the Revenue Acts of 1932 and 1934?

5. Is there any error in the arrangement of the Board's memorandum opinion which discusses separately each of the issues presented, grouping together a recitation of the facts and of the reasoning and conclusions with respect to each issue? The applicable statute is Section 1117 (b) of the Internal Revenue Code.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations are set forth as follows: Those pertaining to the first issue in Appendix A, *infra,* pp. 34–36; those pertaining to the second issue in Appendix B, *infra,* pp. 37–39; those pertaining to the third issue in Appendix C, *infra,* pp. 40–49; those pertaining to the fourth issue in Appendix D, *infra,* p. 50; and those pertaining to the fifth issue in Appendix E, *infra,* p. 51.

STATEMENT

The facts have been partially stipulated. (R. 23–30.) The record also contains oral testimony and exhibits. (R. 86–193.) This recitation of those facts which are pertinent to the issues on appeal will follow in general the arrangement used by the Board of Tax Appeals in its memorandum opinion; that is, certain general facts will be stated first, following which particular facts will be discussed as they pertain to each of the issues on appeal.

Two petitions were filed with the Board of Tax Appeals seeking a redetermination of the normal taxes, additional taxes and negligence penalties asserted by the Commissioner against taxpayer, Wilson

Brothers & Company, a corporation, for the years 1932, 1933 and 1934. (R. 31.) On January 31, 1927, F. A. Wilson and W. T. Wilson formed a partnership under the name of Wilson Brothers & Company, which continued to do business under that name until the taxpayer corporation was formed and took over that business in January, 1929. (R. 32–33.) Taxpayer corporation was organized under Nevada law, with an authorized capital stock of 200,000 shares of a par value of $25 each. Twenty shares were initially purchased by F. A. Wilson for $500 and twenty shares were initially purchased by W. T. Wilson for $500. No other shares have ever been issued. During the years in question the books of taxpayer corporation were kept on the accrual basis. (R. 33.)

(a) *With respect to first issue.*

In its return for 1934, taxpayer took a deduction of $5,000 on account of indebtedness due it from Woodhead Lumber Co. of California which was alleged to be partially worthless in the year 1934. The total debt due it from Woodhead Lumber Co. of California at the beginning of the year was $43,276.06. This debt was secured by collateral consisting of a note of another corporation (Woodhead Lumber Co. of Nevada) for $25,000 and stock of the other corporation having a face value of $37,000. Though there was testimony that the collateral had little or no value, taxpayer continued to do business with Woodhead Lumber Co. of Nevada. The Board concluded that the taxpayer had failed to show that the debt due from Woodhead Lumber Co. of California had become

worthless in the indicated amount, and found no error in the Commissioner's disallowance of the $5,000 deduction claimed. (R. 37–38.)

In its return for 1934, the taxpayer deducted $5,500 on account of a debt alleged to be partially worthless in that amount represented by bonds of Kentucky Fuel & Gas Corporation. The bonds were a first mortgage upon the property of the company, which was an operating company with considerable assets. It went into receivership about 1931. The Board concluded that the record did not give sufficient particulars concerning the acquisition of the bonds or their cost to furnish a basis for the deduction sought and also found that there was nothing to show that the alleged worthlessness had not occurred in a prior year. It pointed out that the bid prices for the bond declined from $74 in 1930 to $5 in 1931, $2 in 1933 and $4.50 in 1934. The Commissioner's disallowance of the deduction was sustained. (R. 40–41.)

The steamship Idaho was constructed under a contract with Henry Wilson, the Charles R. Wilson Estate, Inc., and A. B. Johnson. Though the record is somewhat confused upon the point, the Board determined that the original ownership shares were as follows: Henry Wilson 65/100, Charles R. Wilson Estate, Inc., 25/100 and A. B. Johnson 10/100. (R. 41, 49–50.) The cost of the vessel was $200,000. It was completed about February 6, 1917, and its fair market value at that date was not less than $395,000. At that time Henry Wilson gave away the following shares in the vessel—to his wife, Mary Wilson, 20/100, to his

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son, W. T. Wilson, 5/100, and to his son, F. A. Wilson, 5/100. (R. 41–42.)

On June 6, 1924, Henry Wilson gave his wife the 35/100 interest which he then still owned. In July, 1925, F. A. Wilson and W. T. Wilson bought the 10/100 owned by A. B. Johnson (and wife) for $11,716.67. On January 2, 1929, Mary Wilson, W. T. Wilson and F. A. Wilson conveyed their interests in the Idaho (75/100 of it) to taxpayer corporation without consideration. (R. 42–43.)

The dispute upon this appeal is about the 20/100 interest given to Mary Wilson in 1917 and given by her to the corporation in 1929. The Board determined that it was acquired by the corporation by gift and that its basis in the corporation's hands was the same as the basis of the last preceding owner, who did not acquire it by gift, namely, Henry Wilson. Revenue Acts of 1932 and 1934, Section 113 (a) (2). The Board therefore took as the basis for this interest a pro rata part of the original cost of the vessel, rejecting taxpayer's contention that the basis should be a pro rata part of the value of the vessel at the date when this interest was given to Mary Wilson. (R. 50–51.)

(c) *With respect to third and fourth issues.*

Taxpayer was organized to engage in the business of logging, milling, transportation of and dealings in lumber and operation of steamships. (R. 55–56.) The steamships Oregon and Idaho were acquired in 1929, operated for six months and then laid up. They continued to be laid up through the taxable years 1932, 1933 and 1934, which are the years here in question.

(R. 56.) The taxpayer corporation was preceded by a partnership which had about $1,500,000 invested in its business of logging, lumbering, milling and shipping, and a similar business would have required about that much capital at the time of the hearing. (R. 56.) However, prior to 1932 taxpayer had ceased to carry on a logging, milling and shipping business. Though there was an intention to reenter that business at some time, it was not done during the tax years in question. During those years taxpayer engaged in a small lumber business and allied business. The logging and milling business was a losing business during those years. (R. 56.)

Other particulars of the taxpayer's business for the years in question are as follows (R. 56–57):

Year	Gross sales	Net losses from operations	Dividends from stocks	Undivided profits
1932	$28,725.96	$11,740.89	$18,258.00	$19,309.75
1933	92,262.09	1,341.36	17,541.00	36,732.00
1934	170,239.51	118.75	25,057.00	[1] 60,447.64

[1] Consisting of $25,447.64 shown as undivided profits and $35,000 transferred to capital account. (R. 106, 154.)

The income tax returns filed by taxpayer show the common stock of taxpayer to have been the following amounts on the following dates (R. 57):

January 1, 1929	$696,000
" 1, 1930	746,000
" 1, 1931	800,000
" 1, 1932	2,500,000
" 1, 1933	2,500,000
" 1, 1934	2,500,000
December 31, 1934	2,535,000

However, the only stock ever issued was that in the amount of $1,000 originally issued to W. T. Wilson and

F. A. Wilson. (R. 57.) Cash contributions were made to taxpayer by F. A. Wilson and W. T. Wilson from time to time. With such cash, taxpayer from time to time purchased stocks of domestic corporations. (R. 57.)

The income tax returns of the taxpayer show the following, among other things (R. 57–58):

	December 31		
	1932	1933	1934
Assets			
Cash	$1,106,377.07	$1,022,123.45	$972,147.49
Securities of Domestic Corporations	1,000,943.50	1,032,190.55	1,077,778.05
Liabilities			
Notes payable	200,000.00		
Common stock	2,500,000.00	2,500,000.00	2,535,000.00

However the Board found that those items should have been as follows (R. 58):

	December 31		
	1932	1933	1934
Assets:			
Cash, as shown by Account Books and records	$96,638.23	$9,186.43	$73,707.36
Securities of Domestic Corporations as shown by Books of account and Record (cost)	750,943.50	782,190.55	837,778.05
Securities of Domestic Corporations as shown by Books of account and Record (market value)	439,961.87	777,792.00	810,797.75
Liabilities:			
Notes payable as shown by record			
Common stock per record	1,000.00	1,000.00	1,000.00

The taxpayer's records carried no item of $200,000 notes payable, though such an item appeared in the income tax returns, not only for the year 1932 as shown but also for the years 1929, 1930 and 1931. Taxpayer's records did not show that it possessed any I. O. U.'s. However, large amounts of I. O. U.'s

were included in computing the cash on hand shown in the returns. These I. O. U.'s were given by W. T. Wilson and F. A. Wilson. At the time of the trial, the cash box contained an I. O. U. for $843,438.54 showing two equal items, one purportedly due from W. T. Wilson, the other from F. A. Wilson (R. 58–59.)

A certified public accountant was unable to take trial balances from taxpayer's general ledger at the beginning and end of 1932 and at the end of 1933 and 1934 because the general ledger accounts were incomplete. A balance was accomplished only after Francis Wilson, an officer, furnished the accountant with information concerning the identity of certain additional accounts. One of the items on the books dated January 31 (no year) was labeled "transfer from treasury stock $10,000". W. T. Wilson testified "we put in that much cash to take it up." The ledger of the corporation carried two accounts headed "treasury stock" totaling $250,000 but there was, in fact, no treasury stock. The corporate books did not indicate the years in which the recorded transactions occurred. (R. 50.)

No dividends or salaries to officers were paid by taxpayer between the date of its incorporation and the end of the last taxable year here involved. (R. 59.) No federal income taxes were paid by either W. T. Wilson or F. A. Wilson in the years 1932, 1933 or 1934, except about $150 paid by W. T. Wilson in 1932. (R. 59.)

Taxpayer's books show accounts receivable from F. A. Wilson as follows (R. 59–60):

Year	Charges	Credits	Net Due December 31
1933	$82, 597. 77	$39, 363. 40	$43, 234. 37
1934	62, 199. 38	69, 821. 25	35, 612. 50

On January 2, 1935, F. A. Wilson was credited with $35,612.50 by the purchasers of certain stock. The general ledger trial balance shows a different sum as of December 31, 1933, namely, $28,091.96. (R. 60.)

Accounts receivable from W. Wilson (presumably W. T. Wilson) are shown as $17,717.88, $16,917.88 and $16,917.88 at the ends of the years 1932, 1933 and 1934, respectively. (R. 60.)

The Board concluded that the record was unsatisfactory and often contradictory and that the corporate books were kept in no normal manner. (R. 60.) Primarily, taxpayer was a holding or investment company in the tax years in question, actual business operations being so few and far between that vouchers instead of a cashbook were used to record them. No dividends or salaries to officers were being paid. (R. 60–61.)

The sole stockholders contributed large sums of cash to taxpayer. The testimony of one of them was that such contributions amounted to nearly $1,300,000 though there is much contradiction in the record and that figure is not accepted by the Board. (R. 61–62.) W. T. Wilson testified to the following contributions of cash and other assets: December, 1928, $695,000; January 1, 1929, $50,000; January, 1930, $54,000; Janu-

ary 1, 1931, $480,000; and to the contribution of $1,700,000 in I. O. U.'s. He testified to a transfer of $35,000 from profit and loss to surplus and then from surplus to capital, though there was a net loss from operations. He explained an increase in cash on hand from $56,593.58 in December, 1930, to $1,642,298.24 in December, 1931, by saying "we just put a few I. O. U.'s in the cash box" and that I. O. U.'s were used right along. The two Wilsons for four consecutive years swore to income tax returns showing large amounts of cash which was really not cash at all but I. O. U.'s (R. 62.)

The same sworn statements for four consecutive years represented notes payable of $200,000 contrary to the facts, stocks of domestic corporations in the amount of $250,000 more than was the fact, and a capitalization of the taxpayer from $696,000 to $2,535,000 in excess of what it in fact was. (R. 62–63.) Thus, while no particular statement is worthy of consideration because of the many contradictions, it is apparent that the stockholders did contribute large amounts in cash and other assets with which stock and some bonds were purchased by the taxpayer. (R. 63.)

There was testimony by one witness that $1,500,000 would be needed to carry on in 1939 a business comparable to that carried on by the partnership prior to 1929, but there was no testimony pertaining to the requirements of such a business in the tax years in question, namely, 1932 to 1934. Whereas, the testimony indicates that some lumber business was carried on

during those years, the large lumbering and milling business which the partnership had engaged in was not carried on and there was no showing that the accumulations from securities which were not distributed in the years in question were a business necessity. There was no showing of any intent to resume a business of the size formerly carried on by the partnership nor were any details given as to the real scope of the business which was expected to be undertaken. (R. 63–64.) The failure to make an adequate showing as to alleged future business needs was emphasized by the failure to show the business necessity for the large contributions of cash to the corporation which were invested in securities. The Board concluded that the taxpayer had not satisfied the burden of proving that earnings were not accumulated beyond business needs and that taxpayer was not availed of in the tax years to avoid surtaxes to its stockholders. (R. 65.)

The Board thought its conclusion strengthened by the credits permitted to stockholders which would not have been permitted if the accumulations were needed for business capital and by the fact that the corporation was used by the two stockholders, not wholly for legitimate business purposes, but as a sort of incorporated family pocketbook. (R. 65–66.)

The Board also concluded that taxpayer's method of keeping books and making returns was negligent. It determined that a part of the deficiency obviously was due to this negligence and imposed the 5 percent penalty. (R. 67.)

SUMMARY OF ARGUMENT

1. It is in the Commissioner's discretion to allow or not to allow a deduction for debts alleged to have become partially worthless in the tax year. When the Commissioner has refused to allow such a deduction the inquiry of the Court is limited to the question whether the Commissioner has abused his discretion, that is, whether he has acted arbitrarily and capriciously. An additional requisite for such a deduction is that the taxpayer must have ascertained that the portion of the debt claimed as a deduction became worthless in the tax year for which the deduction is sought. Whether the taxpayer did so ascertain is a question of fact as to which the finding of the Board of Tax Appeals is conclusive if supported by substantial evidence.

Taxpayer claimed that a $43,000 debt due it from Woodhead Lumber Company of California became worthless to the extent of $5,000 in the tax year. It is inherently improbable that the taxpayer could have ascertained with any degree of certainty that so small a part as one-ninth of the debt became worthless in the tax year. The only evidence to support its claim was the interested testimony of one of taxpayer's two stockholders, which was vague and contained an admission that there was substantial security behind the debt. As to bonds of Kentucky Fuel & Gas Corporation alleged to have been partially worthless in the tax year, there was no adequate showing of cost. Furthermore, the taxpayer's own evidence clearly discloses that

the partial worthlessness alleged had occurred prior to the tax year.

Taxpayer did not sustain the burden of proving that either of these debts became worthless to the extent claimed in the tax year and did not show facts indicating that the Commissioner abused his discretion in refusing the deductions.

2. Taxpayer disputes the Board's determination as to the basis for depreciation purposes of a one-fifth interest in the steamship *Idaho* acquired by the taxpayer as a gift from the mother of its two shareholders or acquired by the shareholders as a gift from their mother and contributed by them to the taxpayer's capital. The mother had acquired this interest as a gift from her husband. Taxpayer claims that the basis in the corporation's hands should be the same as it was in the mother's, that is, it should be the fair market value of the property when given to the mother. However, the statute is clear that in the case of two consecutive gifts of the same property, the second donee is required to take the basis of the first donor. In the instant case, that means that the taxpayer's basis for the interest in question is the cost of that interest to the father of taxpayer's shareholders, as the Board found.

3. Taxpayer carried on a small lumber business in the tax years in question. It maintained during those years a very large balance of cash and securities. The income from those securities was not distributed to the two shareholders of taxpayer but was accumulated. That failure to distribute saved the shareholders some

surtaxes. The cash and securities held by taxpayer exceeded taxpayer's current needs for working capital. The explanation that taxpayer intended to greatly expand its business is given only by the interested testimony of one of taxpayer's two shareholders. This testimony was vague and, for adequate reasons advanced by the Board, hardly credible. There is substantial evidence to support the Board's conclusion that the taxpayer was primarily a holding or investment company, that its earnings were accumulated beyond its reasonable business needs, and that it was availed of to avoid the imposition of surtax upon its shareholders.

4. It is a reasonable inference from the record in the instant case that at least a part of the deductions claimed by the taxpayer in its returns and disallowed by the Board of Tax Appeals were claimed because of the carelessness of the taxpayer in keeping its records, making its returns, or studying the applicable statutes and Treasury Regulations. The Board was justified in finding that at least a part of the deficiency was due to negligence. Under the applicable statute, the penalty was properly imposed upon the entire amount of the deficiency.

5. The Board was not required to separate its findings of fact from its opinion. The arrangement of its memorandum opinion was a matter for its own discretion. The arrangement it chose was best calculated to promote a clear understanding of a lengthy and complicated case.

ARGUMENT

I

The Board correctly refused to upset the Commissioner's determination not to allow certain deductions claimed by the taxpayer in 1934 on account of debts alleged to be partially worthless

Section 23 (k) of the Revenue Act of 1934, Appendix A, *infra,* authorizes deductions for debts ascertained to be partially or wholly worthless and charged off accordingly. The allowance of a deduction for a partially worthless debt, as distinguished from a debt which is wholly worthless, is within the Commissioner's discretion. The statutory words are "and when satisfied that a debt is recoverable only in part, the Commis-

in an amount not in excess of t

taxpayer's determination that a specific part of the debt has become worthless, the Commissioner's judgment is controlling. The Commissioner's decision may be upset by the courts only if it cannot be reasonably supported upon any theory, that is, only as it represents arbitrary and capricious action amounting to abuse of discretion. *Olympia Harbor Lumber Co.* v. *Commissioner,* 79 F. (2d) 394 (C. C. A. 9th); *United States* v. *Beckman,* 104 F. (2d) 260 (C. C. A. 3rd), certiorari denied *sub nom. Doty* v. *United States,* 308 U. S. 593; *Stranahan* v. *Commissioner,* 42 F. (2d) 729 (C. C. A. 6th), certiorari denied, 283 U. S. 822; *Commissioner* v. *Liberty Bank & Trust Co.,* 59 F. (2d) 320 (C. C. A. 6th); *Ross* v. *Commissioner,* 72 F. (2d) 122 (C. C. A. 7th); *Clark* v. *Commissioner,* 85 F. (2d) 622 (C. C. A. 3rd).

It has been held repeatedly that, as in the case of a deduction claimed for a wholly uncollectible debt, a deduction for part of a debt will be allowed only if it is shown that that part was ascertained to have become worthless in the taxable year for which deduction is sought. *American Sav. Bank & Trust Co.* v. *Burnet,* 45 F. (2d) 548 (C. C. A. 9th); *Pacific Nat. Bank* v. *Commissioner,* 91 F. (2d) 103, 105 (C. C. A. 9th); *Santa Monica Mountain Park Co.* v. *United States,* 20 F. Supp. 209, 211 (S. D. Cal.), affirmed, 99 F. (2d) 450 (C. C. A. 9th), certiorari granted and dismissed by stipulation of counsel, 306 U. S. 666; *Jones* v. *Commissioner,* 38 F. (2d) 550 (C. C. A. 7th); *Motter* v. *Wallace,* 72 F. (2d) 678 (C. C. A. 10th); *Austin* v. *Helvering,* 77 F. (2d) 373, 374 (App. D. C.); *Johnson, Drake & Piper* v. *Helvering,* 69 F. (2d) 151 (C. C. A. 8th), certiorari denied, 292 U. S. 650.[2]

We think that the same conclusion is compelled by the Treasury Regulations. Article 23 (k)–1 of Treas-

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[2] *Moock Electric Supply Co.* v. *Commissioner,* 41 B. T. A. 1209, quoted from by taxpayer (Br. 26), is not to the contrary. The quotation which taxpayer gives lacks this significant sentence which immediately follows it (p. 1212):

> Total worthlessness or disposition of the obligation remained open to this petitioner as a ground for deduction, notwithstanding the possibility that partial worthlessness may have appeared in an earlier year.

The rationale of the *Moock* opinion and of cases like *Blair* v. *Commissioner,* 91 F. (2d) 992 (C. C. A. 2d), which it cites, is that a taxpayer may wait until a debt is wholly uncollectible before taking any deduction. These cases do not hold that a debt which becomes uncollectible by 50 per cent in year A and is still uncollectible by that amount in year B may be deducted to the extent of 50 per cent in either year A or year B, as the taxpayer may choose.

ury Regulations 86, pertaining to the 1934 Act, Appendix A, *infra,* reads in part:

> Before a taxpayer may charge off and deduct a debt in part, he must ascertain and be able to demonstrate, with a reasonable degree of certainty, the amount thereof which is uncollectible.

The same provision has appeared in all Treasury Regulations from 1921 to date.[3] It has come to have the force of law. *Helvering* v. *Wilshire Oil Co.,* 308 U. S. 90; *Helvering* v. *Winmill,* 305 U. S. 79, 83; *Morgan* v. *Commissioner,* 309 U. S. 78, 81.

If the law were otherwise, a taxpayer who had once ascertained that a debt was worthless in a given amount could take a deduction for that amount in any year thereafter when it best suited him, or, if he chose, could divide the worthless portion up into as many parts as was convenient and take a deduction for one part in each of several years. "The mind rebels against the notion that Congress * * * was willing to foster an opportunity for juggling so facile and so obvious." *Woolford Realty Co.* v. *Rose,* 286 U. S. 319, 330.

It may be observed also that the question "When did the taxpayer first ascertain the partial worthlessness claimed * * *?" is a question of fact. The burden is upon the taxpayer to show that it was ascertained in the year for which the deduction is claimed, and the

[3] Treasury Regulations 62, 1921 Act, Article 151; Treasury Regulations 65, 1924 Act, Article 151; Treasury Regulations 69, 1926 Act, Article 151; Treasury Regulations 74, 1928 Act, Article 191; Treasury Regulations 77, 1932 Act, Article 191; Treasury Regulations 94, 1936 Act, Article 23 (k)–1; Treasury Regulations 101, 1938 Act, Article 23 (k)–1; Treasury Regulations 103, Internal Revenue Code, Section 19.23 (k)–1.

determination of the Board upon the point must be sustained by the Circuit Court of Appeals, if supported by any substantial evidence. *Theatre Inv. Co.* v. *Commissioner,* 119 F. (2d) 477 (C. C. A. 9th); *Uhl Estate Co.* v. *Commissioner,* 116 F. (2d) 403, 405 (C. C. A. 9th); *Person Const. Co.* v. *Commissioner,* 116 F. (2d) 94, 95 (C. C. A. 7th); *Curtis* v. *Helvering,* 110 F. (2d) 1014 (C. C. A. 2d).

In the light of the foregoing analysis, it will be evident that there is no basis for reversal of the decision of the Board which affirmed the disallowance by the Commissioner of claimed deductions for partial worthlessness of the debt due the taxpayer from Woodhead Lumber Company and of the indebtedness represented by Kentucky Fuel & Gas Corporation bonds owned by the taxpayer. Both deductions were claimed in the year 1934.

At the beginning of 1934, taxpayer was owed about $43,000 by Woodhead Lumber Company, and has claimed partial worthlessness of only $5,000, or about one-ninth of the total debt. On its face, this claim would be more reasonable if it was for an addition to bad debt reserve. However, taxpayer admits that it does not have that character. Therefore, taxpayer has left itself with a very difficult burden of proof, that is, the burden of showing, as the applicable regulation (quoted *supra*) requires, that $5,000 may, with a reasonable degree of certainty, be said to be the amount by which this $43,000 debt became worthless in 1934.

The only testimony on that point was the interested testimony of W. T. Wilson, half owner of the taxpayer corporation, appearing at pages 94–96 and 110–111 of

the record. This testimony is obviously of such a confused character as to give no clear picture of the debtor's true condition. Nothing so certain as a balance sheet of the debtor is offered and analyzed. The witness admitted that collateral was held consisting of a $25,000 note of another corporation and $37,000 face amount of the other corporation's stock. It was the Board's function to appraise the testimony of this witness and its judgment that such testimony did not sustain the burden upon taxpayer is binding upon the appellate court. *Helvering* v. *Nat. Grocery Co.,* 304 U. S. 282, 294–295.

Two patent defects appear in the taxpayer's case for a deduction of partial worthlessness of bonds of Kentucky Fuel & Gas Corporation. First, cost was shown only by entries upon the taxpayer's books dated at the end of each year. (R. 127, 170.) The inaccuracy of those books fully appears from that portion of the Board's opinion (R. 54–67) which relates to what we call third issue (discussed *infra* under Point III). The Board was entirely justified in rejecting those book entries in the absence of some substantiating evidence concerning the transactions by which the bonds were acquired and the prices paid for them. Second, the testimony of the accountant, upon which the taxpayer must rely for the claimed deduction, clearly shows that the partial worthlessness claimed had occurred and was ascertained in a prior year. The bonds dropped from a bid price of $74 in 1930 to $5 in 1931, $1.25 in 1932, $2 in 1933, and $4.50 in 1934 (the year in which deduction was claimed). (R. 127–128.)

II

The Board correctly determined that the donee's basis for property which was the subject of two consecutive gifts was the cost to the first donor

The dispute here has to do solely with $^{2}0/_{100}$ interest in the steamship Idaho, which was given by Henry Wilson to his wife on February 16, 1917, and in turn transferred by her to the taxpayer corporation (which was owned by her two sons) in 1929. The question is what basis to assign to the property in taxpayer's hands for depreciation purposes.

The transfer by Mary Wilson to taxpayer corporation amounted either to a gift to the corporation or a gift to F. A. and W. T. Wilson, Mary's sons, and capital contributions by them to taxpayer. If the latter, the capital contributions were tax-free when made. Cf. Treasury Regulations 74, Article 67, Appendix B, *infra*. Consequently taxpayer's basis for the purposes of depreciation computations in 1932, 1933 and 1934, the years here involved, is the basis (with adjustments) of the property in the hands of the Wilson brothers, transferors to the corporation. Revenue Acts of 1932 and 1934, Section 113 (a) (8), 113 (b), and 114 (a), Appendix B, *infra*. Since the Wilson brothers obtained the contributed property by gift in 1929, their basis is to be determined by Section 113 (a) (2) of the Revenue Act of 1928, c. 852, 45 Stat. 791, the pertinent portion of which is unchanged in Section 113 (a) (2) of the Revenue Acts of 1932 and 1934, Appendix B, *infra*.

On the other hand, if the 1929 transfer by Mary Wilson to taxpayer corporation was a gift directly to tax-

payer, then its basis must be determined by Section 113 (a) (2) of the Revenue Acts of 1932 and 1934, Appendix B, *infra*.[4]

Thus either analysis leads to the same basic statutory provision (appearing in Section 113 (a) (2) of the 1928, 1932 and 1934 Acts.) That provision is:

> If the property was acquired by gift after December 31, 1920, the basis shall be the same as it would be in the hands of the donor or the last preceding owner by whom it was not acquired by gift.

The obvious purport of this provision is as follows: If the property is purchased by A and given to B, B shall take A's cost (with adjustments) as his basis; and if property is purchased by A, who gives it to B, who gives it to C, C shall take A's cost (with adjustments) as his basis.

Section 113 (a) (4) of the 1928, 1932 and 1934 Acts provides that property given before 1921 shall have a basis in the donee's hands equal to its fair market value at the time of the gift. Taxpayer argues that where A gives to B before 1921 and B gives to C after 1921, C should take B's basis (value of the property when given to B) instead of cost to A. Such a result ignores the fact that Section 113 (a) (4) has no bearing upon C's basis, which must be determined by Section 113 (a) (2). Such a result would violate the express mandate of the words "the basis shall be the same as it would be in the hands of * * * the last preced-

[4] Point 3 of taxpayer's brief (pp. 27–32) is in error in looking to an earlier statute to determine basis in taxpayer's hands for the purpose of the years 1932, 1933, and 1934.

ing owner by whom it was not acquired by gift" used in Section 113 (a) (2). We believe no further argument is required to demonstrate that the taxpayer's position is wholly untenable.

Taxpayer hints at unconstitutionality, charging a retroactive application of the statute. This charge is based upon the fact that the first of the sequence of two gifts was made prior to 1921, when the above-quoted provisions first appeared in the tax laws (as Section 202 (a) (2) of the Revenue Act of 1921, c. 136, 42 Stat. 227). This is not significant. When the 1929 gift was made by Mary Wilson, the quoted provision was in effect and both donor and donee were upon notice of the basis which the donee would be required to take. Furthermore, Congress could, if it chose, have taxed the entire amount of a gift as income to the donee, either when received or when converted into cash. Donating property costs the donee nothing. Thus, the quoted statutory provision merely provides a method for alleviating the hardship which would result to the donee from assigning a zero basis to gift property. The taxpayer cannot complain about the mechanics employed by Congress in fixing that basis so as to prevent the accrual of tax-free increments of value. *Helvering* v. *Campbell,* decided by the Supreme Court March 31, 1941, not officially reported but found in 1941 C. C. H., Vol. 4, par. 9359; *Helvering* v. *Reynolds,* decided by the Supreme Court May 26, 1941, not officially reported but found in 1941 C. C. H., Vol. 4, par. 9484.

III

The Board's determination that taxpayer corporation was availed of in the years 1932, 1933 and 1934 to avoid surtax upon its shareholders is supported by substantial evidence

The applicable statutes are Section 104 of the Revenue Act of 1932 and Section 102 of the Revenue Act of 1934 (Appendix C, *infra*). They provide, in effect, that the income of a corporation (including dividends received by it) shall be subject to a surtax if the corporation was formed or availed of for the purpose of preventing the imposition of surtax upon its shareholders through the medium of permitting gains and profits to accumulate instead of being distributed. Each statute provides that if a corporation is a mere holding or investment company, or if its gains or profits are permitted to accumulate beyond its reasonable business needs, either of those facts shall be *prima facie* evidence of a purpose to avoid surtax.

In the instant case the Board found that the taxpayer corporation, though not formed to avoid surtax to its shareholders, was availed of for that purpose in each of the years 1932, 1933 and 1934. That determination, and the subsidiary determinations that the corporation was primarily a mere holding or investment company and that its gains or profits were accumulated beyond its reasonable business needs, are determinations which must be affirmed if supported by any substantial evidence; also, since the burden of proof was on the taxpayer, they may be supported by the presumption of correctness of the Commissioner's determination in the absence of adequate rebutting evidence. *Helvering* v.

Nat. Grocery Co., 304 U. S. 282; *Perry & Co.* v. *Commissioner* (C. C. A. 9th), decided May 23, 1941, not officially reported but found in 1941 C. C. H., Vol. 4, par. 9492; *Commissioner* v. *Cecil B. de Mille Productions,* 90 F. (2d) 12 (C. C. A. 9th), certiorari denied, 302 U. S. 713; *R. L. Blaffer & Co.* v. *Commissioner,* 103 F. (2d) 487 (C. C. A. 5th), certiorari denied, 308 U. S. 576; *Almours Securities* v. *Commissioner,* 91 F. (2d) 427 (C. C. A. 5th); *A. D. Saenger, Inc.* v. *Commissioner,* 84 F. (2d) 23 (C. C. A. 5th).

We take the liberty of reproducing for the Court the Rule 50 recomputation made pursuant to the Board's opinion and approved by the Board of the net income of taxpayer corporation and dividends received by the taxpayer in each of the years 1932, 1933 and 1934 (not in the record):

Year	Net income exclusive of dividends	Dividends	Total
1932	($11,624.33)	$18,258.00	$6,633.67
1933	10,908.61	17,541.00	28,449.61
1934	13,905.79	25,057.00	38,962.79

The foregoing figures compare with the following reported in the taxpayer's returns for the indicated years (R. 132–156):

Year	Net income exclusive of dividends	Dividends	Total
1932	($11,740.89)	$18,258.00	$6,517.11
1933	(118.75)	17,541.00	17,422.25
1934	(1,341.36)	25,057.00	23,715.64

The returns of taxpayer's stockholders, W. T. Wilson and F. A. Wilson, are not in the record. From oral

testimony the Board found that neither paid any income tax in the tax years in question except that W. T. Wilson paid about $150 tax in 1932. (R. 59.) Taxpayer seeks to attach significance to the fact that the Commissioner failed to produce the returns of these individuals. (Br. 56.) The burden of proof being upon the taxpayer, any unfavorable inference from failure to produce those returns must redound against the taxpayer rather than the Commissioner. Consequently, for the purposes of this analysis, we are entitled to assume that in each of the years when no tax was paid by individual stockholders, the addition of a single dollar to the income of either would have resulted in tax.

It is apparent that for the years 1933 and 1934 a distribution of taxpayer's earnings would have placed the income of both shareholders in surtax brackets, whether the earnings found by the Board or those reported in taxpayer's returns are used. In 1933 surtaxes started with $6,000 net income and in 1934 with $4,000 net income. Revenue Acts of 1932 and 1934, Section 12. The difference between the two statutes is compensated for, however, by the fact that in computing income subject to surtax, credits for personal exemption and dependents (Sec. 25) are not allowed under the 1932 Act, whereas they are allowed under the 1934 Act. Thus, under either statute we are entitled to assume that a distribution of about $4,000 from the taxpayer corporation to each of its two shareholders would have brought the income of each shareholder into the surtax brackets. The income available for distri-

bution was considerably in excess of $4,000 for each of the two shareholders.

In 1932 it may be assumed, perhaps, that a distribution of earnings would not have resulted in surtax to F. A. Wilson. But it certainly would have put the income of W. T. Wilson into the surtax brackets, for he paid a tax of $150, indicating an income over and above personal exemption and credit for dependents of approximately $3,750. Adding to this amount $3,000 from the taxpayer and an exemption and credit for dependents of, say, $3,000 would give him an income of about $10,000, well within the surtax area.

It cannot be denied, therefore, that surtaxes to the individual shareholders of taxpayer were avoided by not distributing to them the earnings of taxpayer which accumulated in each of the tax years in question. The fact that the surtaxes avoided were small is certainly not conclusive of no purpose to avoid surtax. Equally inconclusive is the fact that in one of the years only one of the two shareholders was saved from surtax by taxpayer's retention of its earnings.

An argument is made (Br. 42–44) that the earnings available for distribution should be deemed reduced by a shrinkage in value of assets such as securities, notes, and accounts receivable. The Board found that taxpayer owned securities in the following amounts in each of the years in question (R. 58):

Year	Market value	Cost
1932	Approximately $440,000	$751,000
1933	" 778,000	782,000
1934	" 810,000	838,000

It is readily apparent that considerable fluctuation in value of such a large block of securities is inevitable and is not material to the issue whether the income from those securities has been withheld from distribution to the shareholders for the purpose of saving them surtaxes. That it is not material has been established by authoritative decisions. *Helvering* v. *Nat. Grocery Co., supra; A. D. Saenger, Inc.* v. *Commissioner, supra.* It is even more readily apparent that that issue is not affected by the fact that taxpayer may have thought certain accounts receivable among its assets were partially worthless, or that certain bonds had declined in value below their cost to the taxpayer. See taxpayer's

tially worthless debts, and
real unnecessarily accumulated

It handled only the following gross lumber business (R. 56, 58):

Year	Gross sales	Cash and securities on hand
1932	$28,725.96	Approximately $536,000.
1933	92,262.09	" 787,000.
1934	170,239.51	" 884,000.

It is also significant that the business carried on by taxpayer made no profit in any of the three years and that the income which accrued and was accumulated in each year resulted from dividends upon its investments in securities. We do not believe that a reasonable argument could be made to the effect that the very large accumulation of cash and securities available to the

taxpayer was necessary to carry on the business which it did in the tax years in question.

Taxpayer's principal claim (Br. 32–61) is that it contemplated a renewal of operations on a very much larger scale, including the operation of its boats and the carrying on of milling and logging business. It points to the testimony of one of its two stockholders that for such a business a capital of $1,500,000 was required.

The Board rightfully deemed that the testimony of taxpayer's shareholder concerning the purpose to expand and the amount of capital which would be required, was inadequate to sustain the burden upon the taxpayer. This testimony appears at pages 101 *et seq.* of the record. It is of a vague and general character. No details of the expansion contemplated are given. No time for the expansion is set or estimated. Though the reason for the restricted business in the tax years was said to be the business depression, there is no testimony that the expansion had occurred at any time prior to the trial in 1939; it is common knowledge that a business recovery had occurred before that time. The testimony concerning the need for capital of $1,500,000 related to the time of the trial. No estimate was made for the capital which would have been necessary to resume the full business in the tax years or immediately thereafter.

In addition to the vagueness of the testimony, the Board was reluctant to give it full credence because of the many inconsistencies in the sworn statements of the witness and his brother. (R. 62–67.) The weight and

credibility of interested testimony of this type is for the Board to determine. If it had so chosen, the Board could have disregarded this testimony altogether. *Helvering* v. *Nat. Grocery Co., supra,* at pp. 494–495.

From the whole record, it was reasonable to infer that in the years 1932 to 1934, inclusive, taxpayer had no such immediate intention to greatly expand as would require the accumulation of securities income on top of the securities and cash already held. It was reasonable to infer that taxpayer was to be used primarily as a holding or investment company, not only in the tax years, as the Board found, but in subsequent years as well. Its large investments in bonds and stocks were accumulated to a great extent out of contributions to the capital of the corporation by its two shareholders. Cf. *Helvering* v. *Nat. Grocery Co., supra; Perry & Co.* v. *Commissioner, supra; R. L. Blaffer & Co.* v. *Commissioner, supra.* It was rather obviously the incorporated pocketbook of the Wilson family. Cf. *R. L. Blaffer & Co.* v. *Commissioner, supra; Almours Securities* v. *Commissioner, supra; A. D. Saenger, Inc.* v. *Commissioner, supra.* The existence of large accounts receivable from its two shareholders in each of the years in question is indicative that the accumulations of earnings were not necessary for working capital. Cf. *Helvering* v. *Nat. Grocery Co., supra; Perry & Co.* v. *Commissioner, supra; A. D. Saenger, Inc.* v. *Commissioner, supra; United Business Corp.* v. *Commissioner,* 62 F. (2d) 754 (C. C. A. 2d), certiorari denied, 290 U. S. 635.

Typical of the taxpayer's protest against the Board's findings is its statement (Br. 53) that there is not a

shred of evidence to support the Board's conclusion that accounts receivable from "W. Wilson" shown on the books were accounts receivable from W. T. Wilson, half owner and treasurer of the taxpayer corporation. Taxpayer, who bore the burden of proof, has not suggested who else "W. Wilson" might be or made any reasonable explanation for loans to some other party than W. T. Wilson.

We submit that there is ample evidence to sustain the Board's determination that taxpayer was primarily a holding or investment company, that earnings were accumulated beyond the reasonable needs of its business, and that it was availed of to avoid surtaxes to its stockholders in the tax years in question.

IV

The Board's imposition of the negligence penalty should be sustained

While the specific items of negligence and resulting deficiency giving rise to the penalty were not recited by the Board, we believe there is substantial evidence to support the Board's conclusions that some part of the deficiency flowed from the taxpayer's negligence. Under the statute, the penalty falls upon the entire deficiency if any part of it is due to negligence. Revenue Acts of 1932 and 1934, Section 293 (a), Appendix D, *infra*.

The negligence penalty certainly is warranted if the taxpayer takes deductions the improper size or character of which would have been revealed by careful bookkeeping or a reasonably careful analysis of the

statutes and regulations. We believe the penalty to be warranted when a deduction is taken, though its propriety can be neither proved nor disproved because of carelessly incomplete records. It is a fair inference from this record that at least some of the deductions disallowed by the Board resulted from careless or incomplete bookkeeping or a failure to make a reasonably careful attempt to follow the law and Treasury rules.

V

The form of the Board's memorandum opinion reveals no error

The Board was not required to make separate fact findings and separately state conclusions of law. No form for a memorandum opinion is specified by statute. Internal Revenue Code, Section 1117 (b), Appendix E, *infra*. *California Iron Yards Co.* v. *Commissioner,* 47 F. (2d) 514, 518 (C. C. A. 9th); *Insurance & Title Guarantee Co.* v. *Commissioner,* 36 F. (2d) 842 (C. C. A. 2d), certiorari denied, 281 U. S. 748; *Emerald Oil Co.* v. *Commissioner,* 72 F. (2d) 681 (C. C. A. 10th). The Board's separate grouping of the facts and discussion pertaining to each issue is, to say the least, helpful to a clear consideration of this case. It is hard to see how this wise arrangement can seriously be criticized, though taxpayer has undertaken to do so. We think taxpayer unwarranted in inferring that the Board, in discussing each issue, closed its mind to the facts and circumstances recited in connection with other issues.

The fair assumption is, we think, that the facts primarily concerning each issue were analyzed by the Board against the background of the entire case.

CONCLUSION

The decision of the Board of Tax Appeals should be affirmed.

Respectfully submitted,

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JUNE, 1941.

APPENDIX A

STATUTE AND REGULATIONS PERTAINING TO FIRST ISSUE

Revenue Act of 1934, c. 277A, 48 Stat. 680:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (k) *Bad Debts.*—Debts ascertained to be worthless and charged off within the taxable year (or, in the discretion of the Commissioner, a reasonable addition to a reserve for bad debts); and when satisfied that a debt is recoverable only in part, the Commissioner may allow such debt, in an amount not in excess of the part charged off within the taxable year, as a deduction.
>
> * * * * *
>
> (U. S. C., Title 26, Sec. 23.)

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

> ART. 23 (k)–1. *Bad debts.*—Bad debts may be treated in either of two ways—
>
> (1) By a deduction from income in respect of debts ascertained to be worthless in whole or in part, or
>
> (2) By a deduction from income of an addition to a reserve for bad debts.
>
> * * * * *
>
> If all the surrounding and attending circumstances indicate that a debt is worthless, either wholly or in part, the amount which is worthless and charged off or written down to a nominal amount on the books of the taxpayer shall be allowed as a deduction in computing net income.

There should accompany the return a statement showing the propriety of any deduction claimed for bad debts. No deduction shall be allowed for the part of a debt ascertained to be worthless and charged off prior to January 1, 1921, unless and until the debt is ascertained to be totally worthless and is finally charged off or is written down to a nominal amount, or the loss is determined in some other manner by a closed and completed transaction. Before a taxpayer may charge off and deduct a debt in part, he must ascertain and be able to demonstrate, with a reasonable degree of certainty, the amount thereof which is uncollectible. Any amount subsequently received on account of a bad debt or on account of a part of such debt previously charged off and allowed as a deduction for income tax purposes, must be included in gross income for the taxable year in which received. In determining whether a debt is worthless in whole or in part the Commissioner will consider all pertinent evidence, including the value of the collateral, if any, securing the debt and the financial condition of the debtor. Partial deductions will be allowed with respect to specific debts only.

* * * * *

ART. 23. (k)–4. *Worthless bonds and similar obligations.*—Bonds, if ascertained to be worthless, may be treated as bad debts to the amount actually paid for them. Bonds of an insolvent corporation secured only by a mortgage from which on foreclosure nothing is realized for the bondholders are regarded as ascertained to be worthless not later than the year of the foreclosure sale, and no deduction for a bad debt is allowable in computing a bondholder's income for a subsequent year.

A taxpayer (other than a dealer in securities) possessing debts evidenced by bonds or other similar obligations can not deduct from gross income any amount merely on account of mar-

ket fluctuation. If a taxpayer ascertains, however, that due, for instance, to the financial condition of the debtor, or conditions other than market fluctuation, he will recover upon maturity none or only a part of the debt evidenced by the bonds or other similar obligations and so demonstrates to the satisfaction of the Commissioner, he may deduct in computing net income the uncollectible part of the debt evidenced by the bonds or other similar obligations.

APPENDIX B

STATUTES AND REGULATIONS PERTAINING TO SECOND ISSUE

Revenue Acts of 1932, c. 209, 47 Stat. 169; and 1934, c. 277, 48 Stat. 680:

The following provisions are identical in the two Acts, except that the italicized portion of Section 113 (a) (2) appears in the 1934 Act only; and of Section 114 (a) in the 1932 Act only.

> SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.
>
> (a) *Basis (Unadjusted) of property.*—The basis of property shall be the cost of such property; except that—
>
> * * * * *
>
> (2) *Gifts after December 31, 1920.*—If the property was acquired by gift after December 31, 1920, the basis shall be the same as it would be in the hands of the donor or the last preceding owner by whom it was not acquired by gift, *except that for the purpose of determining loss the basis shall be the basis so determined or the fair market value of the property at the time of the gift, whichever is lower.* If the facts necessary to determine the basis *in the hands of the donor or the last preceding owner* are unknown to the donee, the Commissioner shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. If the Commissioner finds it impossible to obtain such facts, the basis *in the hands of such donor or last preceding owner* shall be the fair market value of such property as found by the Commissioner as of the date or approximate date at which, according to the best information that the

Commissioner is able to obtain, such property was acquired by such donor or last preceding owner.

* * * * *

(8) *Property acquired by issuance of stock or as paid-in surplus.*—If the property was acquired after December 31, 1920, by a corporation—

(A) by the issuance of its stock or securities in connection with a transaction described in section 112 (b) (5) (including also, cases where part of the consideration for the transfer of such property to the corporation was property or money, in addition to such stock or securities), or

(B) as paid-in surplus or as a contribution to capital, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made.

* * * * *

(b) *Adjusted Basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) *General rule.*—Proper adjustment in respect of the property shall in all cases be made—

(A) for expenditures, receipts, losses, or other items, properly chargeable to capital account, including taxes and other carrying charges on unimproved and unproductive real property, but no such adjustment shall be made for taxes or other carrying charges for which deductions have been taken by the taxpayer in determining net income for the taxable year or prior taxable years;

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent

allowed (but not less than the amount allowable) under this Act or prior income tax laws. * * *

* * * * *

(U. S. C., Title 26, Sec. 113.)

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(a) *Basis for Depreciation.*—The basis upon which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain or loss upon the sale or other disposition of such property.

* * * * *

(U. S. C., Title 26, Sec. 114.)

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 67. *Contributions to corporation by shareholders.*—Where a corporation requires additional funds for conducting its business and obtains such needed money through voluntary pro rata payments by its shareholders, the amounts so received being credited to its surplus account or to a special capital account, such amounts will not be considered income, although there is no increase in the outstanding shares of stock of the corporation. The payments in such circumstances are in the nature of voluntary assessments upon, and represent an additional price paid for, the shares of stock held by the individual shareholders, and will be treated as an addition to and as a part of the operating capital of the company. (See articles 64 and 282.)

APPENDIX C

STATUTES AND REGULATIONS PERTAINING TO THIRD ISSUE

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 104. ACCUMULATION OF SURPLUS TO EVADE SURTAXES.

(a) If any corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there shall be levied, collected, and paid for each taxable year upon the net income of such corporation a tax equal to 50 per centum of the amount thereof, which shall be in addition to the tax imposed by section 13 and shall be computed, collected, and paid upon the same basis and in the same manner and subject to the same provisions of law, including penalties, as that tax.

(b) The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to escape the surtax.

(c) As used in this section the term "net income" means the net income as defined in section 21, increased by the sum of the amount of the dividend deduction allowed under section 23 (p) and the amount of the interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner.

(d) The tax imposed by this section shall not apply if all the shareholders of the corporation

include (at the time of filing their returns) in their gross income their entire distributive shares, whether distributed or not, of the net income of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corporation out of the earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 102. SURTAX ON CORPORATIONS IMPROPERLY ACCUMULATING SURPLUS.

(a) *Imposition of Tax.*—There shall be levied, collected, and paid for each taxable year upon the adjusted net income of every corporation (other than a personal holding company as defined in section 351) if such corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders or the shareholders of any other corporation, through the medium of permitting gains and profits to accumulate instead of being divided or distributed, a surtax equal to the sum of the following:

(1) 25 per centum of the amount of the adjusted net income not in excess of $100,000, plus

(2) 35 per centum of the amount of the adjusted net income in excess of $100,000.

(b) *Prima Facie Evidence.*—The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to avoid surtax.

(c) *Definition of "Adjusted Net Income".*—As used in this section, the term "adjusted net income" means the net income computed without the allowance of the dividend deduction other-

wise allowable, but diminished by the amount of dividends paid during the taxable year.

(d) *Payment of Surtax on Pro Rata Shares.*—The tax imposed by this section shall not apply if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire pro rata shares, whether distributed or not, of the "adjusted net income" of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corporation out of earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his pro rata share, be exempt from tax in the amount of the share so included.

(e) *Tax on Personal Holding Companies.*—For surtax on personal holding companies, see section 351. (U. S. C., Title 26, Sec. 104.)

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

ART. 541. *Taxation of corporation utilized for evasion of surtax.*—Section 104 is designed to discourage the formation or use of a corporation for the purpose of preventing the imposition of surtaxes upon its shareholders, through the device of permitting its gains and profits to accumulate instead of being distributed. If a domestic or foreign corporation is so formed or availed of, it is subject to a tax at the rate of 50 per cent upon its net income in addition to the tax imposed by section 13. However, the additional tax at the rate of 50 per cent does not apply for 1932 or any subsequent taxable year if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire distributive share, whether distributed or not, of the net income of the corporation for such year or years. Any amount so included in the gross income of a shareholder

shall be treated as a dividend received, and any subsequent distribution made by the corporation out of the earnings or profits for such taxable years shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

ART. 542. *Purpose to escape surtax.*—Prima facie evidence of a purpose to escape the surtax exists where a corporation is a mere investment company, where a corporation has practically no business except holding stocks, securities, or other property and collecting the income therefrom or investing therein, or where a corporation other than a mere holding or investment company permits its gains and profits to accumulate beyond the reasonable needs of the business. The statutory presumption that a mere holding or investment company is subject to the additional tax imposed by section 104 may be overcome if the corporation can show, either by reason of the fact that it distributed a large portion of its earnings for the year in question, or that its stock was held not by the members of a family or of a small group but by a large number of persons and in comparatively small blocks, or by other evidence, that it was not availed of for the purpose of preventing the imposition of the surtax upon its shareholders.

The business of a corporation is not merely that which it has previously carried on, but includes in general any line of business which it may legitimately undertake. However, a radical change of business when a considerable surplus has been accumulated may afford evidence of a purpose to escape the surtax. When one corporation owns the stock of another corporation in the same or a related line of business and in effect operates the other corporation, the business of the latter may be considered in substance the business of the first corporation. Gains and profits of the first corporation put

into the second through the purchase of stock or otherwise may therefore, if a subsidiary relationship is established, constitute employment of the income in its own business. To establish that the business of one corporation can be regarded as including the business of another it is ordinarily essential that the first corporation own substantially all of the stock of the second. Investment by a corporation of its income in stock and securities of another corporation is not without anything further to be regarded as employment of the income in its business.

ART. 543. *Unreasonable accumulation of profits.*—An accumulation of gains and profits is unreasonable if it is not required for the purposes of the business, considering all the circumstances of the case. It is not intended, however, to prevent reasonable accumulations of surplus for the needs of the business. No attempt can be made to enumerate all the ways in which gains and profits of a corporation may be accumulated for the reasonable needs of the business. Distributions made by a corporation shortly after the close of its taxable year shall be taken into consideration in determining the reasonableness of the amount of earnings and profits of the corporation retained by it for such year. Undistributed income is properly accumulated if invested in increased inventories or additions to plant reasonably needed by the business. It is properly accumulated if retained for working capital required by the business or in accordance with contract obligations placed to the credit of a sinking fund for the purpose of retiring bonds issued by the corporation. In the case of a banking institution the business of which is to receive and loan money, using capital, surplus, and deposits for that purpose, undistributed income actually represented by loans or reasonably retained for future loans is not accumulated beyond the reasonable needs of the business. The nature of the investment of gains

and profits is immaterial if they are not in fact needed in the business. It is an unreasonable accumulation of gains and profits by corporations with the purpose of enabling their shareholders to escape surtaxes on such gains and profits which subjects such corporations to the additional tax imposed by section 104. Among other things, the financial condition of the corporation at the close of the taxable year and the manner in which its funds are invested at that date, determine the reasonableness of the accumulations.

For the purpose of section 104 the term "net income" means the net income of the corporation as defined in section 21 increased by the sum of (1) the amount received as dividends and allowed as a deduction by section 23 (p), plus (2) the amount of interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner. The Commissioner, or any collector upon direction from the Commissioner, may require any corporation to furnish a statement of its accumulated gains and profits, the name and address of, and number of shares held by, each of its shareholders, and the amounts that would be payable to each, if the income of the corporation were distributed. (See section 148 (c).) [1]

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 102–1. *Taxation of corporation formed or utilized for avoidance of surtax.*—Section 102 imposes a graduated income tax or surtax upon

[1] Amendments of Articles 541, 542, and 543 of Treasury Regulations 77 were made in 1934 by T. D. 4470, XIII–2 Cum. Bull. 151, but they are not of sufficient significance to the present controversy to reproduce here.

any domestic or foreign organization formed or availed of to avoid the imposition of the individual surtax upon its shareholders or the shareholders of any other corporation through the medium of permitting gains and profits to accumulate instead of dividing or distributing them. However, personal holding companies, as defined in section 351, being taxed separately in accordance with the provisions thereof, are excepted from taxation under section 102. The surtax imposed by section 102 applies whether the avoidance was accomplished through the formation or use of only one corporation or a chain of corporations. For example, if the capital stock of the M Corporation is held by the N Corporation so that the dividend distributions of the M Corporation would not be returned as income subject to the individual surtax until distributed in turn by the N Corporation to its individual shareholders, nevertheless the surtax imposed by section 102 applies to the M Corporation, if that corporation is formed or availed of for the purpose of preventing the imposition of the individual surtax upon the individual shareholders of the N Corporation. The surtax is in addition to the taxes levied upon corporations generally by Title I. For the computation of the surtax see article 102–4.

ART. 102–2. *Purpose to avoid surtax.*—The Act provides two prima facie presumptions of the existence of a purpose to avoid surtax. The fact (1) that any corporation is a mere holding or investment company, or (2) that the gains and profits are permitted to accumulate beyond the reasonable needs of the business, constitutes prima facie evidence of a purpose to avoid the individual surtax. A corporation having practically no activities except holding property, and collecting the income therefrom or investing therein, shall be considered a holding company within the meaning of section 102. If the activ-

ities further include, or consist substantially of, buying and selling stocks, securities, real estate, or other investment property (whether upon an outright or a marginal basis) so that the income is derived not only from the investment yield but also from profits upon market fluctuations, the corporation shall be considered an investment company within the meaning of section 102.

The assumed purpose to avoid the individual surtax is subject to disproof by competent evidence like any other question. Proof of the purpose, therefore, depends upon the particular circumstances of each case. In other words, the purpose may be evidenced by circumstances other than the presumptions specified in the Act. A corporation is subject to taxation under section 102 when it is formed or availed of for the purpose of preventing the imposition of the individual surtax regardless of whether it is a mere holding or investment company, or whether the accumulations, if any, are in excess of the business needs. On the other hand, the statutory presumptions will be overcome if the corporation can show, by a disclosure of all the facts, that it was neither formed nor availed of for the purpose of avoiding the individual surtax, but the mere fact that it distributed a large portion of its earnings for the year in question is not sufficient to overcome the presumption. All the circumstances which might be construed as evidence of the purpose can not be outlined. Among other things the following will be taken into consideration in determining the existence of such purpose: (1) Dealings between the corporation and its shareholders such as withdrawals by the shareholders as personal loans or the expenditure of funds by the corporation for the personal benefit of the shareholders and (2) the investment by the corporation of undistributed earnings in assets having no reasonable connection with the business.

ART. 102–3. *Unreasonable accumulation of profits.*—An accumulation of gains and profits (including the undistributed earnings or profits of prior years) is unreasonable if it is not required for the purposes of the business, considering all the circumstances of the case. It is not intended, however, to prevent reasonable accumulations of surplus for the needs of the business if the purpose is not to prevent the imposition of the surtax. No attempt can be made to enumerate all the ways in which gains and profits of a corporation may be accumulated for the reasonable needs of the business. Undistributed income is properly accumulated if retained for working capital needed by the business; or if invested in additions to plant reasonably required by the business; or if in accordance with contract obligations placed to the credit of a sinking fund for the purpose of retiring bonds issued by the corporation. The nature of the investment of gains and profits is immaterial if they are not in fact needed in the business. Among other things, the nature of the business, the financial condition of the corporation at the close of the taxable year, and the use of the undistributed earnings or profits will be considered in determining the reasonableness of the accumulations.

The business of a corporation is not merely that which it has previously carried on, but includes in general any line of business which it may legitimately undertake. However, a radical change of business when a considerable surplus has been accumulated may afford evidence of a purpose to avoid the surtax. If one corporation owns the stock of another corporation in the same or a related line of business and in effect operates the other corporation, the business of the latter may be considered in substance the business of the first corporation. Gains and profits of the first corporation put into the second through the purchase of stock or otherwise

may, therefore, if a subsidiary relationship is established, constitute employment of the income in its own business. To establish that the business of one corporation can be regarded as including the business of another it is ordinarily essential that the first corporation own substantially all of the stock of the second. Investment by a corporation of its income in stock and securities of another corporation is not of itself to be regarded as employment of the income in its business.

The Commissioner, or any collector upon direction from the Commissioner, may require any corporation to furnish a statement of its accumulated gains and profits, the name and address of, and number of shares held by each of its shareholders, and the amounts that would be payable to each, if the income of the corporation were distributed. (See section 148 (c).)

APPENDIX D

STATUTES PERTAINING TO FOURTH ISSUE

Revenue Acts of 1932, c. 209, 47 Stat. 169; and 1934, c. 277, 48 Stat. 680:

SEC. 293. ADDITIONS TO THE TAX IN CASE OF DEFICIENCY.

(a) *Negligence.*—If any part of any deficiency due to negligence, or intentional disregard of rules and regulations but without intent to defraud, 5 per centum of the total amount of the deficiency (in addition to such deficiency) shall be assessed, collected, and paid in the same manner as if it were a deficiency, except that the provisions of section 272 (i), relating to the prorating of a deficiency, and of section 292, relating to interest on deficiencies, shall not be applicable.

* * * * *

(U. S. C., Title 26, Sec. 293.)

APPENDIX E

Internal Revenue Code:

SEC. 1117. REPORTS AND DECISIONS.

* * * * *

(U. S. C., Title 26, Sec. 293.)

(b) *Inclusion of Findings of Fact or Opinions in Report.*—It shall be the duty of the Board and of each division to include in its report upon any proceeding its findings of fact or opinion or memorandum opinion. The Board shall report in writing all its findings of fact, opinions and memorandum opinions.

* * * * *

U. S. GOVERNMENT PRINTING OFFICE: 1941

Nos. 9781 and 9782

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

WILSON BROTHERS AND COMPANY (Wilson Bros. & Co.) (a corporation),
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S REPLY BRIEF.

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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Respondent.

PETITIONER'S REPLY BRIEF.

This brief is in response to the Brief for the Respondent filed in the above-entitled proceedings for review and served on petitioner on July 9, 1941.

A. THE QUESTIONS PRESENTED.

Although respondent has stated the questions in different form than as presented by petitioner (Respondent's Brief pp. 2 and 3) we accept the form and order in which he has presented them and will reply accordingly.

B. RESPONDENT'S STATEMENT OF THE CASE.
(Respondent's Brief, pp. 3-12.)

In making his statement of the case respondent announces that "certain general facts will be stated first, following which particular facts will be discussed as they pertain to each of the issues on appeal." In this feature he follows the error of the Board in its mem-

orandum opinion, of which we complain, by attempting to segregate proven facts and confine them to selected separate issues rather than have all the facts open for consideration where material on all of the issues.

Even while attempting to adopt the scattered findings of the Board, respondent modifies some of their language to benefit his argument. As an instance, the Boards finds: "the petitioner did not reenter the lumber-logging-milling business prior to or during 1932, 1933 and 1934." (R. 56.) Respondent states: "However, prior to 1932 taxpayer had ceased to carry on a logging, milling and shipping business." (Brief p. 7.) This change in language is of considerable assistance to respondent in making his argument to sustain the third question stated in his brief. (p. 2.) It is misleading because petitioner corporation had never engaged in the lumber-logging-milling business, its plans to do so were delayed by the panic of 1929 and the subsequent depression.

As respondent has gone beyond the record in its argument (Brief p. 25) we venture to correct the record as shown by the Board's findings (R. 56) and respondent's statement (Brief p. 7) that: "The taxpayer corporation was preceded by a partnership which had about $1,500,000 invested in its business of logging, lumbering, milling and shipping." Due to faulty reporting in the transcript of evidence, the record fails to show that it was not the immediate predecessor of petitioner that was engaged in such wide spread business with such a large investment but a prior partnership of the same name. It was this older firm that petitioner sought to emulate.

Respondent states that there was no showing of any intent to resume a business of the size carried on by the former partnership, referring to the opinion of the Board only. From the testimony (R. 101, 102) it is clear that the business in mind was at least equal to that of the prior partnership.

Other glaring incidents of enlargement of the effect of the record in attempt to show petitioner liable for surtax are to be found in respondent's statement of the facts. The most reprehensible of these is the statement: "Accounts receivable fom W. Wilson (*presumably W. T. Wilson*) are shown" * * * (Brief p. 10, italics supplied.) There is not one scintilla of evidence to show that W. Wilson and W. T. Wilson were the same person or in any way related, hence the presumption is something unwarranted except for the prosecuting purposes of respondent.

Other discrepancies and misstatements will be pointed out from place to place in the following argument.

C. REPLY ARGUMENT.

I.

THE BOARD ERRED IN SUSTAINING THE COMMISSIONER'S DETERMINATION NOT TO ALLOW CERTAIN DEDUCTIONS CLAIMED BY THE TAXPAYER IN 1934 ON ACCOUNT OF BAD DEBTS ALLEGED TO BE PARTIALLY WORTHLESS.

Under part I of his argument (Brief pp. 16 to 20) respondent consolidates parts I and II of petitioner's argument. (Brief pp. 12-26.) Respondent properly considers the two items covered by his argument as "deductions claimed by the taxpayer in 1934 on account of debts alleged to be partially worthless." How-

ever, he improperly seeks to enlarge the grounds of his defense in order to argue that the Board should be sustained on its denial of such claims.

The respondent having failed by special affirmative allegations in his answer (R. 19) to allege grounds of denial of the claims for deductions made by petitioner is confined to sustaining the Board's action solely upon the grounds for denial thereof found in the deficiency notice. (R. 17.) Petitioner could not be required to do more than submit evidence to overcome the direct reasons expressed by the Commissioner for his denial of the deductions claimed. These reasons were two in number: (1) That no evidence had been submitted to establish the partial worthlessness and (2) no permission had been granted to change from an actual bad debt basis to a reserve basis. As the Board held that "petitioner was on the actual charge-off method of deducting bad debts" (R. 37) the second reason for denial of the claim for deduction has been determined adversely to respondent and requires no further discussion, because it is an issue upon which no error has been assigned.

The task of determining, writing-off and claiming deduction for partially worthless bad debts falls upon the taxpayer and if the surrounding circumstances indicate that the debt is partially worthless and is charged off the amount of the write-off "*shall be allowed* as a deduction in computing net income." (Regulations 86, Art. 23 (k)-1-(2), Petitioner's Opening Brief, p. 16.)

The only point for consideration on the propriety of the deduction is the consideration of the evidence to establish partial worthlessness of the two debts, i. e.

that of Woodhead Lumber Co. of California and that of Kentucky Fuel & Gas Corporation. What evidence the Commissioner had or did not have before him when the deficiency notice for 1934 was prepared we do not know.

Evidence was available to respondent regarding the status of both corporations and it would appear that neither respondent nor his agents performed the duty of checking against such evidence to test the reasonableness of petitioner's claims for deductions. Also, it would appear that respondent had arbitrarily denied the deductions, without effort to ascertain their merit. Furthermore, at the hearing of the proceedings, respondent introduced no evidence to overcome the proofs introduced by petitioner.

Respondent indulges in rather specious statement to bolster his argument to sustain the disallowance of the partial deductions. He seeks to belittle the testimony of W. T. Wilson (Brief p. 19) because he was an interested party, "half owner of the taxpayer corporation". Who would be expected to make an examination, form judgment, and reach a conclusion as to the worthlessness of a debt but someone in close interest to the taxpayer?

Next he misrepresents the amount of security held by petitioner for payment of the indebtedness by stating "The witness admitted that collateral was held consisting of a $25,000 note of another corporation *and* $37,000 face amount of the other corporation's stock". Such a statement leads to the inference that petitioner held collateral amounting to $62,000 or $18,-723.94 in excess of the indebtedness, when such is not the fact. No such admission was made by the witness.

He testified that the note for $25,000 with the stock, which he believed had little value, as collateral for the note had been turned over to petitioner as partial security for the indebtedness. (R. 38. See Petitioner's Opening Brief pp. 18-19.) This left an unsecured indebtedness of $18,276.06 from which the $5,000 was written off. A reading of the record (R. 95) shows that everything essential for the taxpayer to determine the amount of deduction for partial worthlessness had been performed. The finding or determination by the Board of non-deductibility seems to be predicated more upon the fact that petitioner did business with the Woodhead Lumber Co. of Nevada. (R. 38.) The injection or inclusion of this element is gross error, for the deduction was not claimed against the Nevada corporation, which apparently was a solvent corporation with a going business.

With regard to the partial worthlessness of the bonds of the Kentucky Fuel & Gas Corporation respondent defends his action of disallowance on the assertion of what he calls "two patent defects" in petitioner's case. "First, *cost was shown* only by entries upon the taxpayer's books at the end of each year." (Brief p. 20.) If the "cost was shown", as respondent admits, it does not matter whether it was shown in May, June or December. Cost during a specific year was cost of the bonds to petitioner, and that is all the petitioner is required to show. From whom the bonds were purchased, the precise date of purchase, and the other details of purchase are immaterial. "Cost" is the "price paid", although respondent would seem to attempt to create a difference in the meaning. To escape his admission that "cost was shown", respon-

dent seeks to deny the accuracy of the books of account of petitioner. The accuracy and correctness of the cost set up in the books of account was never challenged by respondent during the hearing before the Board, and the differences between the balance sheets in the corporation's income tax return and the books of petitioner did not affect the taxable income of petitioner nor the cost of the bonds. It is interesting to note that the Board accepted petitioner's "cost" as shown by entries on its books of account for all other securities which it owned. (R. 58.)

Respondent next asserts: "Second, the testimony * * * clearly shows that the partial worthlessness claimed *had occurred and was ascertained in a prior year.*" (Brief p. 20.) Such statement is incorrect and not supported by the record cited. (R. 127-128.) It is true that the bonds dropped to a low figure in 1930 and fluctuated at lower prices thereafter, but petitioner had the hopeful right to await a rise or complete collapse in value, and, when neither event happened, to take a write-off for partial worthlessness.

We do not dispute the rules and decisions cited by respondent on pages 16 and 18 of his brief where they are applicable. However, they are not applicable to the conditions of these cases.

We refer to the cases cited in our opening brief (pp. 15-26) as being the applicable authorities for the issues here under argument. In footnote 2 (Brief p. 17) respondent erroneously states and seeks to overcome the rule laid down in *Moock Electric Supply Co. v. Commissioner,* 41 B. T. A. 1209, 1211. (Petitioner's Brief p. 26.) If his contentions are correct, then there could never be a deduction for partial worthlessness

unless the taxpayer had early and definite knowledge of the first trend toward insolvency of a debtor in the first year in which the decline toward insolvency took place. Such contention would nullify the applicable portion of section 23 (k) of the Revenue Act of 1934 and Article 23 (k)-1-(2) of Regulations 86. (Petitioner's Brief p. 16.) The contention conflicts with that portion of Article 23 (k)-1 of Regulations 86 cited by respondent on page 18 of his brief. Before petitioner sought its deductions for partial worthlessness of the two debts it complied with the regulation quoted by respondent. (R. 95, 96.) As the respondent acquiesced to the decision of the Board in *Moock* case (supra) he should not be permitted here to deny the rule which he has accepted.

All that a taxpayer is required to do is to establish a *prima facie* case against respondent on a partially worthless debt, particularly where the grounds stated for disallowances in the deficiency notice are so indefinite and vague as in this case. It has only to show that it has made a reasonable investigation of the facts and drawn a reasonable inference from the information thus obtainable, then the burden of proof passes to respondent. This burden of proof was never undertaken by him.

It must be borne in mind that it is the Commissioner's determination of non-deductibility which is before the Court and that the Board merely affirms the Commissioner. Therefore the closing paragraphs of the opinion in *Clark v. Commissioner,* 85 Fed. (2d) (C. C. A. 3) 622, 625, seem applicable.

> "The taxpayer who knew them" (the circumstances) "at the place and time was in a better

position to make a fair and honest estimate of the value of his security than any one else could possibly be years afterward. The subsequent events show that his estimate was just and reasonable and that the commissioner's is not in accordance with the facts.

"The determination of the commissioner is set aside, the order of re-determination of the Board of Tax Appeals is reversed, and the return of the petitioner reinstated."

II.

THE BOARD IMPROPERLY DETERMINED THAT THE DONEE'S BASIS FOR PROPERTY WHICH WAS THE SUBJECT OF TWO CONSECUTIVE GIFTS WAS THE COST TO THE FIRST DONOR.

This issue is dealt with in Part V-3 (pp. 27-32) of Petitioner's Opening Brief. Respondent is correct in stating that the dispute under this issue has to do solely with 20/100ths interest in the steamship Idaho, which was given by Henry Wilson to Mary H. Wilson, his wife, on February 16, 1917, and transferred by her as a gift to petitioner (which was owned by her two sons) in 1929. The question is what basis to assign to the petitioner as of the date of gift on the 20/100ths interest for purposes of depreciation. (Respondent's Brief p. 21.)

As the second paragraph of respondent's argument on this point seems to be somewhat confusing, we restate it in line with the facts. The transfer by Mary H. Wilson of the 20/100ths interest on January 2, 1929 was a direct gift to the petitioner (R. 93) and, as a gift, was subject to neither gift tax nor income tax. The basis of the value of the gift to petitioner is the

adjusted value to the donor at the time of the gift as determined under section 113 (a) (4) of the Revenue Act of 1928. The provisions of the Revenue Acts of 1932 and 1934 cannot, as respondent seems to argue, affect the depreciable basis of the 20/100ths interest acquired by petitioner in 1929. Such a basis was established at the time of the gift by the Revenue Act then in force and there has been no statutory attempt to provide for a change of such basis. By footnote respondent (Brief p. 22) seeks to obliterate the effect of legislative history recited by petitioner in its opening brief (pp. 29-31). Legislative history is always material in studying the purpose of a development in statutory provisions. We again refer to such history as corroborative of our interpretation of the statute.

If as respondent argues subsection (4) of section 113 (a) is to be ignored as establishing the basis of value of the 20/100ths interest in the steamship "Idaho" in the hands of petitioner on January 2, 1929, and thereafter, why then was that subsection continued in the Act of 1928? Because the gift to Mary H. Wilson was made before January 21, 1921, and on February 6, 1929, she had an unrestricted and continuing vested interest in the property which had an admitted fair market value of 20/100ths of $395,000 on February 6, 1917 (R. 41), the status of that gift was fixed by Section 113 (a) (4) and the basis thereunder was not changed when the property was transferred to petitioner because there is no provision for such change provided by statute. Section 113 provides thirteen methods of ascertaining a basis of value, and excepting where a subsection is restricted or enlarged in effect by reference to other subsection

or section of the Act, each method is independent and self controlling. Subsection (4) does not refer to subsection (2) of section 113, nor *vice versa.*

Respondent seems to be hard driven to sustain his point by speculation of doubtful merit as is demonstrated by his statement (Brief p. 23): "Congress could, if it chose, have taxed the entire amount of a gift to the donee, either when received or when converted into cash." We are not concerned with what Congress might have done but with what it did and what it failed to do. It failed to enact any law which supports respondent's contention on this point.

The cases cited by respondent have no application to the merits of the issue as far as we understand them.

In quoting Section 113 (a) (2) in his argument on page 22, respondent has shown the weakness of his position by deleting the all significant words "the donor or". See petitioner's opening brief pp. 30-32.

III.

THE BOARD'S DETERMINATION THAT TAXPAYER CORPORATION WAS AVAILED OF IN YEARS 1932, 1933 AND 1934 TO AVOID SURTAX UPON ITS SHAREHOLDERS IS NOT SUPPORTED BY ANY SUBSTANTIAL EVIDENCE, BUT IS CONTRARY TO THE CONCLUSIVE EVIDENCE.

Respondent urges generally (Brief pp. 24-25) that the determination of the Board of Tax Appeals on this issue must be sustained because the similar determination made in the deficiency notice is *prima facie* correct, because petitioner was primarily a holding or investment company, and accumulated earnings and profits beyond its reasonable business needs, either of which is *prima facie* evidence of a purpose to avoid

surtax, but by his silence on this score concedes that there was no direct evidence from which even an inference of a purpose or intent to avoid surtax can be drawn. (*Note.* In the second tabulation on page 25 of respondent's Brief, he has transposed the figures of "Net income exclusive of dividends" for 1933 and 1934. See Brief p. 7.)

Respondent urges that any unfavorable inference to be drawn from the fact that the shareholders' returns were not introduced in evidence must operate against petitioner. (Brief p. 27.) Petitioner cannot accede to this. The returns were in respondent's possession and were not in the possession of or made available to petitioner.

Respondent assumes (Brief pp. 26-27) that under either the 1932 or 1934 Revenue Acts a distribution of $4,000 of petitioner's earnings in 1933 and 1934 to each shareholder would have brought each shareholder within surtax brackets. The record does not disclose what losses the shareholders had to offset this distribution and respondent's assumption is unwarranted except as showing the maximum of possible surtax liability which could have been avoided.

However, *en arguendo,* let us see where respondent's assumptions lead. In the first place respondent's assumptions are incomplete because he does not state and the Board did not find what amount should have been distributed by petitioner to produce dividends. Certainly petitioner would not be required to distribute its entire earnings, particularly in view of its recognized business purpose and its impaired bonds and accounts receivable. Furthermore its actual earnings for tax purposes have not yet been determined, let alone its distributable income.

If petitioner's contentions as to distributable income being reduced by additional depreciation, the impairment of bonds and accounts receivable are correct, as they seem to be, virtually no surtax was avoided. (See petitioner's opening brief pp. 42-43.)

On the other hand, the *maximum* of tax liability, on the basis of respondent's assumptions (Brief p. 27), *assuming all earnings and profits as determined by the Board* to be distributable, was approximately as follows:

	1932	1933	1934
W. T. Wilson	$375.00	$220.00	$1,190.00
F. A. Wilson	none	220.00	1,190.00

Respondent states (on the basis of his assumptions) that some surtax was in fact avoided and urges that the pettiness of the avoidance is conclusive of nothing. This might possibly be true if that fact were the sole evidence in the case, but it is not and directly confirms the positive uncontradicted oral testimony which the Board chose to disregard. Certainly for the purpose of avoidance to exist it must be necessary that something existed which it was desired to avoid. Here that something is at the greatest so inconsequential, particularly to persons of means such as petitioner's shareholders, that the avoidance purpose is inconceivable. Under the law of common sense it is inconceivable that petitioner or its stockholders would deliberately incur the corporation penalty liability for the surtax respondent seeks to impose, when the stockholders' surtax, on respondent's own assumptions, would be so small.

As to petitioner's earnings and profits available for dividends respondent urges (Brief p. 28) that other courts have determined a decline in market values of

stocks as being immaterial. His cited authorities deal with cases in which no business purpose or need for the cash equivalent of the stocks has been shown to exist. Here the business purpose when the time came for its consummation, required an investment in cash of a great deal more than petitioner's securities would bring. The obvious purpose of the frequent contributions of cash to the petitioner and the petitioner's acquisition of stocks therewith was to obtain an enlarged capital in order to fulfill that purpose.

Respondent further urges that it is even more apparent that what petitioner thought with respect to the impairment of its bonds and receivables is immaterial. But when we are dealing with a purpose we are dealing with intent and what the taxpayer thought. If the taxpayer and its shareholders thought its income was nil, as far as intent and purpose is concerned, it was nil.

C. H. Spitzner & Son, Inc., 37 B. T. A. 511, 519-523;

Dill Manufacturing Co., 39 B. T. A. 1023, 1030.

Respondent lists the petitioner's gross sales of lumber on page 28 of his brief. Petitioner accedes that for the business actually conducted no reasonable need existed for any considerable amount of liquid assets, despite the fact that under the efforts of petitioner and its officers lumber sales increased from $28,725.96 in 1932 to $170,239.51 in 1934. This increase is distinctly confirmatory of petitioner's purpose and endeavor to greatly enlarge the scope of its operations as shown by the testimony in the record.

Respondent in effect urges that a contemplated business expansion is not a business purpose and that the testimony of the plan of expansion was somewhat

vague. (Brief pp. 28-29.) Confessedly the time for petitioner's intended expansion could not be fixed in advance, it depended upon the improvement in business conditions in the lumber and shipping industries which were sorely affected by the depression which continued through the years involved. Similarly and because the time of such expansion could not be fixed in advance of such change of circumstances neither could the details of asset acquisition and cost be predetermined. Petitioner's officer-shareholders were not gifted with prescience, they were not astrologers or prophets—they were business men engaged in a business in which they had been engaged since 1906 and which they desired to enlarge as soon as in their judgment enlargement was practical at whatever cost would then be necessary to accomplish the desired enlargement.

The testimony of taxpayer's shareholder was not vague and was of a somewhat general character only because of necessity under the foregoing circumstances. It was direct and to the point and was not even made the subject of cross-examination. Taxpayer's purpose was to engage in the lumber and shipping business to the full extent its stockholders had contemplated when the corporation was organized; to the same extent it had been carried on by a predecessor partnership which had had over $1,500,000 invested therein. This purpose would require expense on reconditioning petitioner's steamers, "laid-up" in the summer of 1929 because during the depression they could not be operated at a profit. Timberlands and mill properties would have to be acquired and expensive logging equipment purchased.

Logging roads would have to be constructed. Costs had increased.

Confirmatory of petitioner's business purpose, found as a fact by the Board (R. 36), was its maintenance of its steamers in substantial repair so that they could easily and quickly be recommissioned at any time. (*N. B.* The findings isolated to determine that issue [II of the Memorandum Opinion, R. 35] were not as firmly restated in determining this issue.) Petitioner was endeavoring to increase its lumber sales and did increase them by 600 per cent in the years involved. Petitioner's shareholders were constantly enlarging petitioner's liquid assets by cash contributions, kept invested in liquid assets so that the desire for expansion could be met whenever the right time came. (See petitioner's opening brief pp. 48-50.)

Respondent states that as a matter of common knowledge a business recovery had occurred prior to 1939. (p. 29.) This was not in the shipping or lumbering business nor applicable to the taxable years under review and certainly was not of the character to warrant the risk at any time prior to 1940 of a million and a half dollars or more in those industries.

Certainly it is true that the weight and credibility to be accorded testimony is a matter for the discretion of the Board. But when that testimony is strongly substantiated by accepted facts, when the facts testified to are the only ones which can be correlated with the accepted facts, it is an abuse of discretion not to follow that testimony. This is particularly true when the stated reason for the refusal is that errors were

made and sworn to on the balance sheets incorporated in petitioner's income tax returns, errors which could result in no possible detriment to anyone, least of all respondent. (See petitioner's opening brief pp. 50-51.)

On page 28 of his brief respondent states: "It is also significant that the business carried on by petitioner made no profit in any of the three years and that the income which was accrued and was accumulated in each year resulted from dividends upon its investments in securities." Is respondent confessing error? The Board determined that petitioner's income for 1933 and 1934, exclusive of dividends was, respectively, $10,908.61 and $13,905.79 (see respondent's brief p. 25) and this despite the fact that extensive depreciation and repairs were held deductible with respect to the steamers, productive of no income. Petitioner reported a gross profit from sales for those years of $8,424.60 and $20,152.56, respectively. (R. 142, 153.)

Respondent has asserted his business judgment as superior to that of petitioner's officers who had been engaged in the lumber business thirty-four years at the date of hearing when he attempts to state (p. 30) what amount of cash and securities would be required by petitioner's business purpose. He *infers* that the expansion was not immediately intended during the years 1932 to 1934 and that implying, in effect, petitioner could have distributed its earnings and the shareholders could have later contributed the distributions back again. But why such circuity when the eventual purpose always existed?

Respondent states that petitioner was rather obviously the incorporated pocketbook of the Wilson family, but does not say how or why. To us it is anything but obvious. In what transactions did petitioner's shareholders deal with it as an incorporated pocketbook? It neither borrowed from or loaned to either of them during any year before the Board.

Respondent speaks of *large* accounts receivable from the two shareholders during the years 1932 to 1934. As to "W. Wilson" he is assuming again. Until the writing of briefs respondent was silent as to the account receivable of "W. Wilson" as being something different from the other accounts receivable shown on petitioner's Exhibit 18. (R. 171-173.) As to F. A. Wilson he is ignoring the fact that the accounts receivable represented the balance on F. A. Wilson's books as a stock broker in favor of petitioner, F. A. Wilson was buying and selling securities for petitioner as its broker, not borrowing money from it. (R. 178.) (See also, petitioner's opening brief pp. 53-56.)

Petitioner submits that the Board committed error in determining this issue against petitioner, and that it should be reversed.

IV.

THE BOARD'S IMPOSITION OF THE NEGLIGENCE PENALTY IS CLEAR ERROR AND CANNOT BE SUSTAINED.

Respondent's argument on this point (Brief p. 31) is so weak as to be a tacit admission that it is without merit or hope. Not a single point of petitioner's argument on this issue (Brief pp. 61-70) has been met or refuted. Respondent states (Brief p. 32):

> "We believe the penalty to be warranted when a deduction is taken, *though its propriety can be neither proved nor disproved* because of carelessly kept records. It is a fair inference from this record that at least some of the deductions disallowed by the Board resulted from carelessness or incomplete bookkeeping or a failure to make a reasonably careful attempt to follow the law and Treasury Rules." (Italics supplied.)

In the deficiency notices respondent asserts the penalty only as "attributable to negligence." (R. 19, 224.) Now he argues nothing about negligence and pleads for a "fair inference" on an unfair ground which has nothing to do with "negligence." Mistakes in seeking deductions are common because of the confusion of the law and respondent here argues that if a taxpayer erroneously seeks a deduction because of uncertainty as to the year or amount for which it should be taken he is to be penalized. Such a position is not one to be commended by this Court.

V.

THE FORM OF THE BOARD'S MEMORANDUM OPINION IS ERRONEOUS.

We quite agree with respondent that the Board is not required to make separate findings of fact and separately state conclusions of law. Nor is any form for a memorandum opinion specified by statute. However, the Board is required to make findings of the facts upon which it basis its opinion.

> *Diller v. Commissioner,* (C. C. A. 9) 91 Fed. (2d) 194, 195.

Furthermore such findings of fact where generally applicable may not be restricted so that their effect is denied to pertinent issues.

Brampton Woolen Co. v. Commissioner, (C. C. A. 1) 45 Fed. 327, 328.

We charge the Board with isolating its findings in some of the issues so as to render them applicable only to such issues when they are momentous to others and, also, in making no findings on other issues excepting by reference to immaterial facts found specifically for another issue. This is certainly error.

As an instance in making its findings on issue V (R. 54) relating solely to the liability of petitioner for surtax for accumulation of surplus no finding is made concerning any negligence of petitioner within the contemplation of section 293 (a) of the Revenue Acts of 1932 and 1934. Yet in determining issue VI (R. 67) the Board's memorandum opinion makes its findings in connection with the discussion of section 104 "applicable with at least equal force" to issue VI. This is not proper finding.

D. CONCLUSION.

It is respectfully submitted that the decision of the Board of Tax Appeals should be reversed to the extent of the errors assigned by petitioner.

Dated, San Francisco,
July 16, 1941.

ADOLPHUS E. GRAUPNER,
LOUIS JANIN,
Counsel for Petitioner.

No. 9790

United States

Circuit Court of Appeals

For the Ninth Circuit.

GEORGE T. GOGGIN, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt,

Appellant,

vs.

BOLSA CHICA OIL CORPORATION, a corporation, THOS. W. SIMMONS, ALLAN A. ANDERSON, WILLIAM H. CREE, H. H. McVICAR, C. M. ROOD and M. M. McCALLEN CORPORATION, a corporation,

Appellees.

Transcript of Record

Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

NO. 9790

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[Clerk's Note: When deemed likely to be of an important nature errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS

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JOSEPH J. RIFKIND, Esq.,
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For Appellees:

MESSRS. OVERTON, LYMAN & PLUMB,
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Los Angeles, California;
Attorneys for Appellees Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson.

ELIZABETH R. HENSEL,
WILLIAM H. CREE, Esq.,
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Los Angeles, California;
Attorneys for Appellees William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation. [1*]

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*Page numbering appearing at foot of page of original certified Transcript of Record.

In the District Court of the United States for the Southern District of California, Central Division.

In Bankruptcy No. 26685-Y

Proceedings for Composition or Extension Under Section 74 of the Bankruptcy Act.

In the Matter of

JACK DAVE STERLING,

Debtor.

DEBTOR'S PETITION

To the Honorable Judges of the Above Entitled Court:

The petition of Jack Dave Sterling, of 3750 Effingham Place, Los Angeles, County of Los An- [2] geles, State of California, Southern District, respectfully represents:

I.

That your petitioner has resided for the greater portion of six months next immediately preceding the filing of this petition at 3750 Effingham Place, Los Angeles, in the County of Los Angeles, State of California, within said judicial district.

II.

That he is unable to meet his debts as they mature and that he desires to effect a composition or extension of time to pay his debts under Section 74 of the Bankruptcy Act as amended.

III.

That your petitioner has been unable to prepare schedules containing a full, true and accurate statement of all assets and liabilities and the names and places of residence of his creditors. That said schedules are being prepared and that the same will be filed within ten days following the filing of this petition.

IV.

That for some time past your petitioner has been and now is engaged in the business of drilling for, producing, marketing and distributing oil in the Southern District of California; that petitioner has conducted said oil business through and by means of seven separate corporate organizations, the names of which are as follows: [3]

1. The Huntington Shore Oil Company;
2. Tide Petroleum Company;
3. Huntington Investment Corporation;
4. Olmstead Petroleum Corporation;
5. E. L. Olmstead Oil Company;
6. Lion Petroleum Corporation;
7. Hill Petroleum Corporation.

That said corporations are the alter ego of your petitioner; that your petitioner is the sole owner thereof and of all of the outstanding shares thereof, and that the directors and officers thereof other than your petitioner are merely nominees and trustees for your petitioner. That the assets and obligations of said companies are so interwoven that serious

injustice will result to your petitioner and the creditors of said corporations and of petitioner if said corporate entities are not disregarded. That it is the desire of your petitioner that all of said corporations, together with all the property thereof and of your petitioner be administered by the above entitled Court as a whole and that said corporate entities be disregarded.

V.

That The Huntington Shore Oil Company is the owner of a certain oil well known as The Huntington Shore Well, and Tide Petroleum Company is the owner of a certain oil well known as the Tide Well, which wells are on adjacent premises located in the Huntington Beach oil field in the County of Orange, State of California, in said Southern Dis-
[4] trict of California; that said oil wells are now on production and are capable of producing one thousand (1,000) barrels of oil per day.

VI.

That said Huntington Investment Corporation is the owner of four oil wells, to-wit, Huntington Investment No. 1a, Huntington Investment No. 2, E. L. Olmstead McKenzie No. 1 and E. L. Olmstead McKenzie No. 2. Said four wells are located in the Signal Hill oil field, in the County of Los Angeles, State of California, in said Southern District of California, and are at the present time off produc-

tion. Said four wells have been involved in certain actions in the Superior Court of the State of California, in and for the County of Los Angeles, wherein certain adjoining and nearby landowners have alleged that said wells have trespassed upon and under their property; that a stipulation has been entered into in said actions that said wells will not be produced from the present location, but that the same will be surveyed and if found to trespass on other lands will be plugged back to the property from which your petitioner has the legal and lawful right to produce; that your petitioner intends that said stipulation shall be carried into effect.

VII.

That said Lion Petroleum Corporation is the owner of a certain oil well known as Lion No. 1, located in said Signal Hill oil field, which well is [5] now on production and is capable of producing approximately four hundred barrels of oil per day.

VIII.

That said Hill Petroleum Corporation is the owner of an oil lease in said Signal Hill oil field, and is now drilling thereon a well known as Hill Petroleum No. 1, which well is at a depth of approximately thirty-seven hundred (3,700) feet.

IX.

That as above set forth, all of said corporations are the alter ego of your petitioner and that their

affairs are intermingled to such an extent that a segregation thereof would be impracticable and would work a great injustice upon the creditors of your petitioner; that your petitioner is not insolvent, but is unable to meet his obligations as they mature, and that there are a great many outstanding obligations and your petitioner is now threatened with attachment and foreclosure proceedings by creditors and unless an extension of time is given your petitioner, his assets will be dissipated and wholly lost, to the irreparable injury of your petitioner and his creditors.

X.

That your petitioner's financial condition and the nature and condition of his assets and liabilities are such that the need for reorganization is essential and compelling and can best be adequately, expediently and economically effected only under the direc- [6] tion and control of this Court; that this petition is filed in good faith and is neither collusive nor for the purpose of obtaining any preference or improper advantage for any one creditor, or any party in interest, or any class of parties in interest, over any other creditor, or any other party in interest, or any other class of parties in interest, save as such classes are lawfully entitled to such preferences, if any, by virtue of liens or securities; that this debtor is informed and believes and therefore alleges that a great majority of the

creditors desire as does your petitioner the assistance of this Court in effecting such reorganization.

XI.

That if your petitioner is left in charge and possession of his assets, he has agreed with the larger creditors that said creditors may select a creditors' committee and that said creditors' committee will supervise the operations of the debtor's property and generally control all receipts and disbursements in respect thereto, pending the submission of a plan of extension or composition by your petitioner. That your petitioner proposes only to operate said producing wells and to sell the oil therefrom, pending the meeting of creditors in the above entitled matter, and does not intend to operate said wells involved in said trespass actions as above alleged.

Wherefore, your petitioner prays that his petition be approved by the above entitled court and [7] that proceedings be had in accordance with the provisions of Section 74 of the Bankruptcy Act as amended; that pending further proceedings in the above entitled matter your petitioner prays that the above entitled Court enter an order allowing your petitioner to remain in control of the above described properties and that all creditors, marshals, sheriffs and attorneys be restrained from proceeding with any action of any character affecting your petitioner's assets, and particularly the properties described in this petition, and that your petitioner

be granted a period of ten days from the filing of this petition in which to prepare and file herein his schedules setting forth a statement of his assets and liabilities and the names and places of residences of his creditors, and that your petitioner be granted such other and further relief as may be just and proper in the premises.

JACK DAVE STERLING
Petitioner
THOMAS REYNOLDS
FRANCIS B. COBB
Attorneys for Petitioner

United States of America
Southern District of California

Central Division
State of California
County of Los Angeles—ss.

Jack Dave Sterling, being the above named debtor mentioned and described in the foregoing [8] petition, does hereby make solemn oath that the statements therein contained are true to the best of my knowledge, information and belief.

JACK DAVE STERLING

Subscribed and sworn to before me this 14th day of October, 1935.

[Seal] VINCEL GARNER
Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Filed 1:30 Oct. 14, 1935. R. S. Zimmerman, Clerk.

[Title of District Court and Cause.]

ORDER APPROVING DEBTOR'S PETITION UNDER SECTION 74 AND RESTRAINING ORDER.

Upon reading and filing the verified petition of Jack Dave Sterling, debtor in the above entitled matter, and it appearing therefrom that the debtor has filed a voluntary petition under Section 74 of the Bankruptcy Act, as amended, and the same having been presented to and considered by this Court, and it appearing from said petition that the debtor is a proper person and party to file a petition under said Section 74, and that he has resided in the Southern District of California, Central Division at 3750 Effingham Place, Los Angeles, California, for more than six months next preceding the filing of said petition, and it further appearing that said [9] debtor is solvent, but is unable to meet his obligations as they mature, and that he desires to effect a composition or extension of time to pay his debts, and the Court being satisfied that the petition has been filed in good faith, and having been fully advised in the premises.

Now, Therefore, on motion of Thomas Reynolds and Francis B. Cobb, attorneys for the debtor,

It Is Ordered:

1. That said petition be and it is hereby approved as having been filed in good faith, and in accordance with Section 74 of the Bankruptcy Act as amended.

2. That within ten days from the date of this Order the above named debtor file his verified schedules of his assets and liabilities, as provided by law, with the above entitled Court; and the debtor is hereby granted said period of ten (10) days from the date hereof within which to file the same.

3. That the above named debtor remain in possession and control of the properties and assets described in his petition, as well as his other property wheresoever located, pending a meeting of creditors.

4. That all persons, firms and creditors, including all creditors of the above named debtor and of the corporations named in said petition, their representatives, attorneys and servants and all sheriffs, marshals and other officers and their deputies, representatives and servants, and all other persons [10]whomsoever, be and they hereby severally are enjoined and restrained from instituting or proceeding with any suit or action of any character involving or affecting any of the assets and property described in the petition or any assets and property in the possession of or owned by the above named debtor or any of said corporations, or in which the above named debtor has an interest; and said parties are severally further enjoined from proceeding with any action now pending, or procuring the appointment of any receiver, or from taking or attempting to take into their possession any of said assets or properties, or from inter-

fering in any way with the possession thereof by the debtor.

5. That this Court reserves full right of jurisdiction to make from time to time such orders as the Court may deem proper in respect to the operation of the business of the debtor, and the fixing of a reasonable time within which claims of the respective parties may be filed and determined, and to modify or limit this order.

Dated this 14th day of October, 1935.

LEON R. YANKWICH
Judge of the above entitled court.

[Endorsed]: Filed Oct. 14, 1935. R. S. Zimmerman, Clerk. [11]

[Title of District Court and Cause.]

PETITION BY DEBTOR FOR ADJUDICATION.

To the Honorable Leon Yankwich, Judge of the Above Entitled Court:

The verified petition of Jack Dave Sterling respectfully shows:

I.

That he has heretofore filed a petition under Section 74 of the Bankruptcy Act as amended.

That the Court entered an order allowing your petitioner to remain in charge of his assets pending the calling of a meeting of creditors.

That your petitioner has been operating under

the supervision of a creditors' committee appointed by Earl E. Moss, Referee in said proceeding, and also under a Receivership, which receiver was appointed by the above entitled Court.

II.

That your petitioner has submitted to the larger creditors a draft of the debtor's proposal, and has had an audit made of his books and records, as well as of the corporations referred to in the debtor's original petition on file.

That your petitioner finds that the larger creditors have recovered preferences within four months prior to the filing of the proceeding. That they are unwilling to agree upon a plan whereby each of [12] them will surrender said preferences and their securities.

That your petitioner finds that he is unable to procure the agreement of the different classes of creditors in respect to the amounts and classification of their claims.

That a large amount of time has been expended in endeavoring to work out a proposal that would be acceptable to the required number of creditors. That after diligent effort your petitioner has been unable to receive any assurance that he can obtain the consent of his creditors to any proposal.

That your petitioner's creditors are demanding that they be given a day in court and that some action be taken.

III.

That your petitioner has concluded that he is helpless to proceed with a proposal that will meet the approval of his creditors, and that further delay and expense will be entailed if a hearing is had and a proposal is made which will not be approved by the required number of creditors.

That your petitioner has decided to, and does hereby petition the above entitled Court to adjudge him a bankrupt, pursuant to subdivision "1" of section 74 of the Bankruptcy Act as amended.

IV.

That your petitioner has heretofore prepared schedules as required by the Bankruptcy Act as [13] amended as to all of your petitioner's assets and liabilities, as well as the assets and liabilities of the corporations referred to in the debtor's original petition. That said corporations referred to in said petition are filing voluntary petitions in bankruptcy with the above entitled Court, in order that all of the assets may be under the custody and control of the above entitled court, and in order that the administration may be had of said assets in an equitable and economic manner.

Wherefore your petitioner prays that the above entitled Court enter an order adjudicating your petitioner to be a bankrupt pursuant to the Acts of Congress relating to Bankruptcy, as amended.

JACK DAVE STERLING

Petitioner.

FRANCIS B. COBB

Attorney for Petitioner.

United States of America
Southern District of California
County of Los Angeles—ss.

I, Jack Dave Sterling, the petitioning debtor mentioned and described in the foregoing petition, do hereby make solemn oath that the statements contained therein are true according to the best of my knowledge, information and belief.

JACK DAVE STERLING
Petitioner.

Subscribed and sworn to before me this 22nd day of November 1935.

[Seal] FRANCIS B. COBB
Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Filed Nov. 23, 1935. Earl E. Moss, Referee. Phyllis Gray, Clerk.

[Endorsed]: Filed Nov. 26, 1935. R. S. Zimmerman, Clerk.

[Title of District Court and Cause.]

ADJUDICATION AND ORDER OF REFERENCE

(Under Section 74 Bkcy. Act)

At Los Angeles, in said District, on November 26, 1935, before said Court in Bankruptcy, the Certificate of the Referee that Jack Dave Sterling, Debtor under Section 74 of the Bankruptcy Act in the

above entitled matter should be adjudged bankrupt within the true intent and meaning of the Acts of Congress relating to bankruptcy having been heard and duly considered, the said Jack Dave Sterling, is hereby declared and adjudged bankrupt accordingly.

It is thereupon ordered that said matter be referred to Earl E. Moss, Esq., one of the referees in bankruptcy of this court, to take such further proceedings therein as are required by said Acts; and that the said Jack Dave Sterling shall attend be- [15] fore said referee on December 3, 1935 at his office in Los Angeles, California, at 10 o'clock a. m., and shall submit to such orders as may be made by said referee or by this Court relating to said matter in Bankruptcy.

Witness, the Honorable Wm. P. James, Judge of said Court, and the seal thereof, at Los Angeles, in said District on November 26, 1935.

R. S. ZIMMERMAN,

Clerk

By L. WAYNE THOMAS

Deputy Clerk

[Endorsed]: Filed Nov. 26, 1935. R. S. Zimmerman, Clerk. [16]

[Title of District Court and Cause.]

ORDER OF RE-REFERENCE

It appearing to the Court that E. R. Utley, Esq., has been duly appointed and has qualified as Referee in Bankruptcy for the Southern District of California to take the place of Earl E. Moss, Esq.

It Is Ordered that the above entitled cases be and they hereby are re-referred to E. R. Utley, Esq., as Referee in Bankruptcy, to take such further proceedings therein as are required by the Acts of Congress relating to bankruptcy.

Dated: Apr 1 1936

WM. P. JAMES
U. S. District Judge

[Endorsed]: Filed Apr. 1, 1936. [17]

[Title of District Court and Cause.]

APPOINTMENT OF TRUSTEE BY CREDITORS

At Los Angeles, in said District, on the 6 day of January, 1936, before Earl E. Moss, Referee in Bankruptcy.

This being the day appointed by the Court for the first meeting of creditors in the above bankruptcy, and of which due notice has been given in the Los Angeles Daily Journal, we, whose names are hereunder written, being the majority in number and in amount of claims of the creditors of the

said bankrupt, whose claims have been allowed, and who are present at this meeting, do hereby appoint Hubert F. Laugharn, of Los Angeles, in the County of Los Angeles, and State of California, to be the trustee of the said bankrupt's estate and effects, and suggest a bond in the sum of $100,000.00.

Signature of Creditors	Amount of Debt
Oil Tool Exchange, Ind.	$ 349.47
J. D. Rush	2,658.59
	5,658.59
Standard Pipe & Supply Co.	5,256.49
Baash-Ross Tool Co.	1,026.26
Baker Oil Tool	1,395.00

By R. Dechter

It Is Hereby Ordered that the above Appointment of Trustee be, and the same is approved, and all claims filed at or before this meeting are hereby allowed unless otherwise noted on said claims.

It Is Further ordered that before said Trustee shall take into his possession any property of this estate exceeding in value the amount of his bond as above set forth he shall file and have approved a bond equal to the value of the said property.

EARL E. MOSS
Referee in Bankruptcy

[Endorsed]: Filed Apr. 3, 1941. R. S. Zimmerman, Clerk. [18]

[Title of District Court and Cause.]

APPOINTMENT OF TRUSTEE BY CREDITORS

At Los Angeles, in said District on the 7th day of January, 1941, before Ernest R. Utley, Referee in Bankruptcy,

Hubert F. Laugharn, Trustee herein, having filed his resignation as such trustee, and this being the day appointed by the Court, for the meeting of creditors to elect a new Trustee under the said Bankruptcy, and of which due notice has been given to the creditors and interested parties herein, we, whose names are hereunder written, being the majority in number and in amount of claims of the creditors of the said bankrupt, whose claims have been allowed, and who are present at this meeting, do hereby appoint George Goggin, of Los Angeles, in the County of Los Angeles, and State of California, to be the trustee of the said bankrupt's estate and effects, and suggest a bond in the sum of $25,000.00.

Signature of Creditors	Amount of Debt
Oil Well Supply Company	$116,568.40

JOSEPH RIFKIND
Attorney for Oil Well
Supply Company.

It Is Hereby Ordered that the above Appointment of Trustee be, and the same is approved.

It Is Further Ordered that before said Trustee shall take into his possession any property of this estate exceeding in value the amount of his bond

as above set forth he shall file and have approved a bond equal to the value of the said property.

ERNEST R. UTLEY
Referee in Bankruptcy.

[Endorsed]: Filed Apr. 2, 1941. R. S. Zimmerman, Clerk. [21]

[Title of District Court and Cause.]

PETITION OF TRUSTEE IN BANKRUPTCY FOR INSTRUCTIONS RELATIVE TO HUNTINGTON SHORE WELL

Comes Now Hubert F. Laugharn and respectfully represents and petitions as follows:

I

That he is the duly appointed, qualified and acting Trustee in Bankruptcy in the above entitled matter.

II

That the Bolsa Chica Oil Corporation, a corporation, has commenced the redrilling of that certain oil well commonly known and designated as "Petroleum Well" at Huntington Beach, California, covered by Easement No. 290-1 granted by the State of California.

III

That petitioner is informed and believes and on that ground alleges that the proposed course of redrilling said "Petroleum Well" will cause the same to come within one hundred (100) feet of the

"Huntington Shore Well" of the above entitled bankrupt estate, which is situated on that certain real property in the County of Orange, State of California, more particularly described as follows:

> Lot Two (2) in Block Three Hundred Nineteen (319) of Huntington Beach Seventeenth Street Section in the City of Huntington Beach, as per Map recorded in Book 4, Page 10 of Miscellaneous Maps, Records of said County,

covered by Easement No. 309-21 granted by the State of California. [23]

IV

That petitioner is further informed and believes and on that ground alleges that the surveys, as plotted, and their intersection with the inclined planes show that it will be impossible to redrill the "Petroleum Well" without coming within one hundred (100) feet of the oil sands perforated by and from which production is obtained by the "Huntington Shore Well", particularly at thirty-seven hundred (3700) feet, thirty-eight hundred (3800) feet, thirty-nine hundred (3900) feet and four thousand (4000) feet, and thereby causing infiltration of oil, mud, cement and other foreign substances, and that the same will result in irreparable damage to and possible loss of said "Huntington Shore Well".

V

That said "Huntington Shore Well" was placed on production on August 15, 1937. The average daily production for the past twelve (12) months has been approximately two hundred ninety-five

(295) barrels per day. The estimated value of said well is Three Hundred Fifty Thousand ($350,000.00) Dollars. That attached hereto and made a part hereof is an affidavit of Vernon L. King, a geologist and petroleum engineer who was employed in connection with the redrilling of the "Huntington Shore Well" and as such, is familiar with the underground course and oil sands from which said "Huntington Shore Well" is producing. That attached hereto and made a part hereof is also an affidavit of Jack Dave Sterling, under whose direction the "Huntington Shore Well" was redrilled and who, because of his many years of practical experience in the oil business, together with his familiarity by reason of the redrilling of the said "Huntington Shore Well", is familiar with the conditions thereof.

Wherefore, your petitioner, by reason of the value of said well and the irreparable loss and damage which will probably result thereto by reason of the redrilling of the said [24] "Petroleum Well", desires that the court give instructions to said petitioner as to the action and proceedings which should be taken by the Trustee in Bankruptcy in the matter.

HUBERT F. LAUGHARN
Trustee in Bankruptcy

JOSEPH J. RIFKIND and
RAPHAEL DECHTER
By JOSEPH J. RIFKIND
By.....

Attorneys for Trustee in Bankruptcy

United States of America
Southern District of California
Central Division—ss.

Hubert F. Laugharn, being by me duly sworn, deposes and says: that he is the Petitioner in the above entitled action; that he has read the foregoing Petition of Trustee in Bankruptcy for Instructions Relative to Huntington Shore Well and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon his information or belief, and as to those matters that he believes it to be true.

HUBERT F. LAUGHARN

Subscribed and sworn to before me this 20th day of April, 1940.

[Seal] PHYLLIS GRAY

Notary Public in and for the County of Los Angeles, State of California. [25]

[Title of District Court and Cause.]

AFFIDAVIT OF VERNON L. KING IN CONNECTION WITH PETITION OF THE THE TRUSTEE IN BANKRUPTCY FOR INSTRUCTIONS RELATIVE TO HUNTINGTON SHORE WELL.

State of California
County of Los Angeles—ss.

Vernon L. King, being first duly sworn, deposes and says:

That he is and for the past twenty-three (23) years has been a geologist and petroleum engineer; that for the past twelve (12) years he has been a consulting engineer in Southern California; that he acquired his education as a geologist and petroleum engineer at Department of Mining and Geology of Stanford University and graduated therefrom in 1917.

That affiant has made an examination and analysis of the surveys, plats, courses, charts and other data which is on file with the Division of Lands of the State of California showing the course of the Petroleum Well at Huntington Beach, California, covered by Easement No. 290-1 granted by the State of California, which is and for several months last past has been off production and which the Bolsa Chica Oil Corporation has commenced to redrill.

That affiant has also made an examination and analysis of the plats, courses, charts and other data which is on file with the Division of Lands of the State of California showing the course of the Huntington Shore Well at Huntington Beach, California, covered [26] by Easement No. 309-2a, granted by the State of California.

That the surveys of said wells are made by independent and impartial experts and technicians engaged and specializing in surveying and plotting the underground courses of oil wells. That affiant was the consulting geologist and petroleum engineer employed in connection with the redrilling of the Huntington Shore Well, and as such is intimately

familiar with the underground course and oil sands from which said Huntington Shore Well is producing.

That the surveys, as plotted, and their intersection with the inclined planes, show, in affiant's opinion, that it will be impossible to redrill the Petroleum Well without coming within one hundred (100) feet of the oil sands perforated by and from which production is obtained by the Huntington Shore Well, particularly at thirty-seven hundred (3700) feet, thirty-eight hundred (3800) feet, thirty-nine hundred (3900) feet and four thousand (4000) feet, and thereby, in affiant's opinion, causing infiltration of oil, mud, cement and other foreign substances which will, in affiant's opinion, result in irreparable damage to, if not possibly the loss of, the well.

That the Bolsa Chica Oil Corporation commenced the redrilling of said Petroleum Well *or* or about April 15, 1940. That said Huntington Shore Well is drilled at an angle into the tidelands of the State of California under easement, as previously stated, and for that reason any change in the gas pressure or shifting of underlying oil sands makes remedial work exceedingly difficult and extremely hazardous.

That said Huntington Shore Well was placed on production on August 15, 1937, the average daily production of said Huntington Shore Well, for the past twelve (12) months, has been approximately two hundred ninety-five (295) barrels per day, that the fair and [27] reasonable value of said Hunting-

ton Shore Well, in affiant's opinion, is approximately Three Hundred Fifty Thousand ($350,000.00) Dollars.

VERNON L. KING

Subscribed and sworn to before me this 18th day of April, 1940.

[Seal] HERTHA N. EBERT

Notary Public in and for the County of Los Angeles, State of California. [28]

[Title of District Court and Cause.]

AFFIDAVIT OF JACK DAVE STERLING IN CONNECTION WITH PETITION OF TRUSTEE IN BANKRUPTCY FOR INSTRUCTIONS RELATIVE TO HUNTINGTON SHORE WELL

State of California
County of Los Angeles—ss.

Jack Dave Sterling, being first duly sworn, deposes and says:

That he has been engaged in the oil business in Southern California for the past 8 years; that the "Huntington Shore Well" of the above entitled bankrupt estate was originally drilled and thereafter redrilled under the direction and supervision of affiant; that in addition to the personal knowledge of the course and formations through which said "Huntington Shore Well" was drilled, affiant has made *and* examination of plats, course charts

and other data showing the course of the "Huntington Shore Well" at Huntington Beach, California, covered by Easement No. 309-2a granted by the State of California, and also of the course of "Petroleum Well" at Huntington Beach, California, covered by Easement No. 290-1 granted by the State of California.

That from affiant's personal knowledge of the course and formations through which said "Huntington Shore Well" was drilled and confirmed by his examination and analysis of plats, course charts and other data examined by him in connection with the "Huntington Shore Well" and the "Petroleum Well", it is affiant's opinion that [29] said "Petroleum Well" cannot be redrilled without coming within one hundred (100) feet of the oil sands perforated by and from which production is obtained by the "Huntington Shore Well", and it is affiant's further opinion that the redrilling of the "Petroleum Well" will cause infiltration of oil, mud, cement and other foreign substances in the "Huntington Shore Well", resulting in irreparable damage to and possible entire loss of said "Huntington Shore Well."

That the "Huntington Shore Well" was placed on production on August 15, 1937; that the average daily production of said "Huntington Shore Well" for the past twelve (12) months has been approximately two hundred ninety-five (295) barrels per day; that the fair and reasonable value of said "Huntington Shore Well" is, in affiant's

opinion, approximately Three Hundred Fifty Thousand ($350,000.00) Dollars.

JACK DAVE STERLING

Subscribed and sworn to before me this 19th day of April, 1940.

[Seal] BEATRICE M. FOREMASTER

Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Filed Apr. 20, 1940. Ernest R. Utley, Referee, By Blanche Morris, Clerk.

[Endorsed]: Filed Jan. 30, 1941. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

[30]

[Title of District Court and Cause.]

ORDER TO SHOW CAUSE ON PETITION OF TRUSTEE IN BANKRUPTCY FOR INSTRUCTIONS RELATIVE TO HUNTINGTON SHORE WELL

Upon reading the verified petition of Hubert F. Laugharn, as Trustee in Bankruptcy in the above entitled matter, together with the affidavit of Vernon L. King, geologist and petroleum engineer, and the affidavit of Jack Dave Sterling, and good cause appearing therefrom,

It Is Ordered that the Bolsa Chica Oil Corporation, a corporation, be and appear before Honorable Ernest R. Utley, Referee in Bankruptcy, 327 Federal Building, Temple and Spring Streets, Los An-

geles, California, on the 26 day of April, 1940, at 2 o'clock P. M., then and there to show cause, if any it has, why such order or orders should not be made and entered by the above entitled court in the above entitled matter to protect the "Huntington Shore Well" of the above entitled bankrupt estate from damage resulting from the redrilling of the "Petroleum Well", and why such additional further and future order or orders should not be made and entered authorizing the Trustee in Bankruptcy to institute, maintain and prosecute any action, proceedings or suit in this or any other court which may, in the opinion of the Trustee in Bankruptcy, be necessary or advisable to protect the "Huntington Shore Well" from damage as the result of the redrilling of the "Petroleum Well."

It Is Further Ordered by the above entitled court, [31] that a copy of the petition of Hubert F. Laugharn, as Trustee in Bankruptcy, and the affidavit of Vernon L. King and the Affidavit of Jack Dave Sterling, be served concurrently with the service of this order.

Dated: April 20, 1940.

ERNEST R. UTLEY
Referee in Bankruptcy

[Endorsed]: Filed Apr. 20, 1940. Ernest R. Utley, Referee. Blanche Morris, Clerk.

[Endorsed] Filed Jan. 30, 1941. R. S. Zimmerman, Clerk. By Louis J. Somers, Deputy Clerk.

[32]

[Title of District Court and Cause.]

INJUNCTION AGAINST BOLSA CHICA OIL CORPORATION, ET AL.

The verified petition of Hubert F. Laugharn, as Trustee in Bankruptcy in the above entitled matter, and the order to show cause issued thereon directed to the Bolsa Chica Oil Corporation, a corporation, came on regularly for hearing before Hon. Ernest R. Utley, Referee in Bankruptcy, on April 26, 1940, at two o'clock P. M. and after being partially heard on said date, was continued for further hearing to and the hearing thereof was concluded on May 1, 1940, at two o'clock P. M. The Trustee in Bankruptcy appeared through and was represented by Joseph J. Rifkind and Raphael Dechter, his attorneys, and the Bolsa Chica Oil Corporation, a corporation, appeared through and was represented by Cecil A. Borden and Warren S. Pallette, of Overton, Lyman & Plumb, its attorneys. The Bolsa Chica Oil Corporation, upon the calling of the matter, announced that it was appearing specially for the sole purpose of objecting to the jurisdiction of the court to make any order affecting said corporation; that thereupon the court informed counsel that it would withhold ruling upon the question of jurisdiction until sufficient evidence was introduced to determine the question; that oral and documentary evidence was introduced upon the part of the Trustee in Bankruptcy and the witnesses called on behalf of the Trustee in Bankruptcy were cross-

examined by the attorneys for the Bolsa Chica Oil Corporation; the Bolsa Chica Oil Corporation, having at the conclusion of the introduction of oral and documentary evidence upon behalf of the Trustee in Bankruptcy, [33] stipulated in open court to the granting of the injunction as hereinafter more particularly set forth, the Bolsa Chica Oil Corporation stating that such stipulation was subject to the objection to the jurisdiction of the court and that such stipulation was not intended to confer general jurisdiction on the court; the court having been fully advised in the premises and the court having overruled the objection of Bolsa Chica Oil Corporation to the jurisdiction of the court,

It Is, Therefore, Ordered as Follows:

That the Bolsa Chica Oil Corporation, its superintendent, agents and employees, shall be and they hereby are restrained and enjoined from drilling, redrilling or sidetrackings its "Petroleum Well", also known as "Fee No. 1 Well", at Huntington Beach, California, so that it comes closer than 200 feet from the "Huntington Shore Well" of said bankrupt estate, measured on a horizontal plane, at any point below the depth of 3800 feet below sea level as the course of the "Huntington Shore Well" is shown on the plat or chart offered and received in evidence and marked Trustee's Exhibit 5.

That in determining whether such drilled, redrilled or sidetracked portion of "Petroleum Well", also known as "Fee No. 1 Well", approaches within 200 feet of the "Huntington Shore Well" shall

be conclusive as to the parties as the same is delineated on said plat and the distance therefrom shall be conclusively determined by plotting the course of the drilled, redrilled or sidetracked portion of said "Fee No. 1 Well" on said plat, based upon single shot surveys taken during the course of the drilling, redrilling or sidetracking of the "Petroleum Well", also known as "Fee No. 1 Well", at approximately every 100 feet, which single shot surveys shall be made available to the Trustee in Bankruptcy or his representatives as the same are from time to time taken and made. [34]

That the circulating fluid used in drilling, redrilling or sidetracking of said "Petroleum Well", also known as "Fee No. 1 Well", shall be virgin crude oil maintained at a grade and gravity consistent with good oil practice in said field, and that no mud or other foreign substances of any kind shall be used in lieu or as part of such circulating fluid, provided that a substitute circulating fluid may be used as may be mutually agreed to in writing between the petroleum engineers for the respective parties thereto.

That there shall be no cementing of said "Petroleum Well", also known as "Fee No. 1 Well", nor shall any cement be used in connection with the drilling, redrilling or sidetracking thereof unless written consent is first obtained from the petroleum engineer representing the Trustee in Bankruptcy, provided that if the petroleum engineer for the parties cannot agree as to whether such proposed cementing will be detrimental to the "Huntington

Shore Well" or not, then and in that event the matter may, upon notice to the respective parties, be submitted for determination at a hearing before the Division of Oil and Gas of the State of California.

That nothing in this order is intended to nor shall any provision of this order preclude or in any manner whatsoever impair the right of the Trustee in Bankruptcy to institute, maintain or prosecute any plenary action, proceeding or suit in any court of competent jurisdiction concurrently, consecutively or cumulatively for injunctive relief or to recover any damages which may be sustained by the "Huntington Shore" by reason of the drilling, redrilling or sidetracking of the "Petroleum Well", also known as "Fee No. 1 Well."

Dated this 15th day of May, 1940.

ERNEST R. UTLEY
Referee in Bankruptcy [35]

Approved as to Form and Contents:

JOSEPH J. RIFKIND and
RAPHAEL DECHTER
By JOSEPH J. RIFKIND
Attorneys for Trustee in Bankruptcy

OVERTON, LYMAN & PLUMB
By CECIL A. BORDEN
Attorneys for Bolsa Chica Oil Corporation, a corporation.

[Endorsed]: Filed May 15, 1940. Ernest R. Utley, Referee. Phyllis Gray, Clerk.

[Endorsed]: Filed Dec. 31, 1940, 12:03 P. M. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [36]

[Title of District Court and Cause.]

PETITION TO HAVE BOLSA CHICA OIL CORPORATION, ET AL., CERTIFIED FOR CONTEMPT, ETC.

Comes now Hubert F. Laugharn and respectfully represents and petitions as follows:

I.

That he is the duly appointed, qualified and acting trustee in bankruptcy in the above entitled matter. That one of the assets of said bankrupt estate is that certain oil well commonly known and designated as "Huntington Shore Well" situated in the County of Orange, State of California, and more particularly described as follows:

> Lot Two (2) in Block Three Hundred Nineteen (319) of Huntington Beach Seventeenth Street Section in the City of Huntington Beach, as per Map recorded in Book 4, Page 10 of Miscellaneous Maps, Records of said County, and

covered by Easement No. 309-2A granted by the State of California.

II.

That heretofore and pursuant to the hearing of a verified petition filed by the trustee in bankruptcy and the Order to Show Cause issued thereon, an injunction was granted on May 15, 1940, against the Bolsa Chica Oil Corporation, its superintendent, agents and employees providing "that

the circulating fluid used in the drilling, redrilling or side-tracking of its "Petroleum Well", also known as "Fee No. 1 Well", shall be virgin crude oil maintained at a grade and gravity consistent with good oil practice in said field and that no [37] mud or other foreign substances shall be used in lieu of or as part of said circulating fluid, provided that a substitute circulating fluid may be used as may be mutually agreed to in writing between the pertoleum engineers for the respective parties thereto."

III.

That the trustee in bankruptcy has been informed by Jack Dave Sterling, who is in charge of the operation of said "Huntington Shore Well", that redrilling operations have been resumed on the said "Petroleum Well", also known as "Fee No. 1 Well", and that mud is being used as a circulating fluid in the redrilling in direct violation of said injunction heretofore issued. That a copy of said injunction was served upon the Bolsa Chica Oil Corporation and its attorneys in said proceedings and a notice of the entry of said injunction against the Bolsa Chico Oil Corporation was served on or about May 17, 1940. That no petition for review was filed and no appeal was taken from the entry and issuance of said injunction within the time provided by law or otherwise, or at all, and that said injunction now is and for several months last past has been final and in full force and effect.

IV.

That some agreement or arrangement has been entered into by and between the Bolsa Chica Oil Corporation, McVicar Rood, Inc., a corporation, M. M. McCullum Corporation, a corporation, H. H. McVicar, C. M. Rood, M. M. McCullum, Thomas W. Simons, "John Doe" Anderson, and Warren S. Pallette and William H. Cree, their attorneys, as a subterfuge, scheme and device to circumvent, evade and escape the force and effect of said injunction, and redrilling operations upon said "Petroleum Well", also known as "Fee No. 1 Well", have been or are about to be resumed with the use of mud as a circulating fluid in violation of said injunction heretofore issued and in force and *a*ffect.

V.

That the trustee in bankruptcy is of the opinion and be- [38] lieves and therefore states that the value of said "Huntington Shore Well" is $350,-000.00. That prior to the commencement of the redrilling operations by the Bolsa Chica Oil Corporation of its "Petroleum Well", also known as "Fee No. 1 Well", that said "Huntington Shore Well" had produced an average daily production over a period of twelve (12) months for the past twelve (12) months preceding the redrilling of said "Petroleum Well", also known as "Fee No. 1 Well", of 296 barrels per day. That as a result of the redrilling operation by the Bolsa Chica Oil

Corporation of its "Petroleum Well", also known as "Fee No. 1 Well", it was necessary to shut down the operation of the "Huntington Shore Well" because of the infiltration of the mud which was being used by the Bolsa Chica Oil Corporation in its redrilling and a column of mud stood in the "Huntington Shore Well" ranging from 1900 feet to 3600 feet, that it was necessary for the trustee in bankruptcy to pull, bale, wash and incur other expenditures for material and labor in an endeavor to preserve and protect the said "Huntington Shore Well" from the damage resulting from the infiltration of said mud used as a circulating fluid in such redrilling, and the trustee in bankruptcy has heretofore sustained damages as a result of the loss of production and remedial work of approximately $10,000.00 and will continue to sustain further damages and loss with the probability of said well being irreparably damaged or injured unless the use of mud as a circulating fluid in said redrilling of said "Petroleum Well", also known as Fee No. 1 Well", is permanently restrained, prohibited and enjoined.

Wherefore, the trustee in bankruptcy prays that Bolsa Chica Oil Corporation, McVicar-Rood, Inc., a corporation, M. M. McCullum Corporation, a corporation, H. H. McVicar, C. M. Rood, M. M. McCullum, Thomas W. Simmons, "John Doe" Anderson, William H. Cree and Warren S. Pallette be certified for contempt to the United States District [39] Court for violating and aiding and abetting in

the violation of said injunction and that in addition thereto, or in the alternative thereof, that the injunction heretofore issued be modified and extended to include each and all of said persons, their agents, servants, employees, successors and assigns, and that pending the hearing of said Order to Show Cause that said persons, and each of them, their agents, servants, employees, successors and assigns, be restrained and enjoined from using of mud as a circulating fluid in the redrilling of said "Petroleum Well", also known as "Fee No. 1 Well".

HUBERT F. LAUGHARN,
Trustee in Bankruptcy.

JOSEPH J. RIFKIND and
RAPHAEL DECHTER,
By JOSEPH J. RIFKIND,
Attorneys for Trustee.

United States of America,
Southern District of California,
Central Division—ss.

Hubert F. Laugharn, being by me first duly sworn, deposes and says: that he is the Trustee in Bankruptcy in the above entitled action; that he has read the foregoing Petition to Have Bolsa Chica Oil Corporation, et al. Certified for Contempt, Etc., and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon

information or belief, and as to those matters he believes it to be true.

HUBERT F. LAUGHARN

Subscribed and sworn to before me this 22nd day of August, 1940.

[Seal] MEREDITH KEITH,

Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Filed Aug. 22, 1940 at 30 min. past 4 o'clock P. M. Ernest R. Utley, Referee. Meredith Keith, Clerk.

[Endorsed]: Filed Dec. 31, 1940—12:03 P. M. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [40]

[Title of District Court and Cause.]

ORDER TO SHOW CAUSE ON PETITION TO HAVE BOLSA CHICA OIL CORPORATION, ET AL., CERTIFIED FOR CONTEMPT, ETC.

Upon reading the verified petition filed by Hubert F. Laugharn as trustee in bankruptcy in the above entitled matter, and good cause appearing therefrom,

It Is Ordered that Bolsa Chica Oil Corporation, McVicar-Rood, Inc., a corporation, M. M. McCullum Corporation, a corporation, H. H. McVicar, C. M. Rood, M. M. McCullum, Thomas W. Simmons, "John Doe" Anderson, and William H. Cree and Warren S. Pallette be

and appear before Hon. Ernest R. Utley, Referee in Bankruptcy, Room 324, Federal Building, Los Angeles, California, on the 30th day of August, 1940, at 10:00 o'clock A. M., then and there to show cause why they and each of them should not be certified to the United States District Court for contempt for violating or aiding or abetting in the violation of the injunction issued against the Bolsa Chica Oil Corporation, et al., on May 15, 1940, in the above entitled matter.

It Is Further Ordered that said persons, and each of them, show cause at said time and place, if any they have, why the said injunction should not be modified, amended and supplemented to include said persons and each of them, and that pending the hearing of this order to show cause, said persons, each and all of them, their agents, servants, employees, successors and assigns be and they are hereby restrained, prohibited and enjoined from using mud as a circulating fluid in the redrilling of the "Petroleum Well", also known as "Fee No. 1 Well", at Huntington Beach, California.

Dated this 22 day of August, 1940.

ERNEST R. UTLEY,
Referee in Bankruptcy. [41]

[Endorsed]: Filed Aug. 22, 1940, at 30 min. past 4 o'clock PM. Ernest R. Utley, Referee. Meredith Keith, Clerk.

[Endorsed]: Filed Dec. 31, 1940, 12:03 PM. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [42]

[Title of District Court and Cause.]

PETITION FOR AUTHORITY TO INSTITUTE SUIT AGAINST BOLSA CHICA OIL CORPORATION.

Comes now Hubert F. Laugharn and respectfully represents and petitions as follows:

I.

That he is the duly appointed, qualified and acting trustee in bankruptcy in the above entitled matter. That one of the assets of said bankrupt estate is that certain oil well commonly known and designated as the "Huntington Shore Well", at Huntington Beach, California. That on or about the 15th day of April, 1940, the Bolsa Chica Oil Corporation commenced the redrilling of its "Petroleum Well", also known as "Fee No. 1 Well", at Huntington Beach, California. That as a result of the infiltration of mud which was being used by the Bolsa Chica Oil Corporation in the redrilling of its said well, it was necessary to shut down the operation of said "Huntington Shore Well" and to pull, bale, wash and incur other expenditures for material, labor and technical assistance in endeavoring to preserve and protect said well from damage and in an endeavor to repair, remove and remedy the damage sustained as a result of the redrilling operations as aforesaid.

II.

That the trustee in bankruptcy has heretofore sustained as a result of said damages from said redrilling operations on account of loss of production and remedial work the sum of approximately $12,540.00, and the trustee in bankruptcy will continue to sustain [43] loss and damage as a result of the permanent and irreparable diminution of production from said well as a result of said redrilling operations estimated at approximately $250,000.00. That a copy of the proposed complaint for damages against the Bolsa Chica Oil Corporation, which the trustee in bankruptcy intends to file upon receiving authority so to do, is attached hereto.

Wherefore, the trustee in bankruptcy prays that he be authorized and empowered to institute action against the Bolsa Chica Oil Corporation for the recovery of the damages sustained and to be sustained by the "Huntington Shore Well" resulting from said redrilling operations as aforesaid and to incur at the expense of the bankrupt estate all costs, charges and expenses arising out of, incidental to and connected with the said litigation.

HUBERT F. LAUGHARN
Trustee in Bankruptcy
JOSEPH J. RIFKIND and
RAPHAEL DECHTER
By JOSEPH J. RIFKIND
Attorneys for Trustee in Bankruptcy

United States of America
Southern District of California
Central Division—ss.

Hubert F. Laugharn, being by me first duly sworn, deposes and says: that he is the Petitioner in the above entitled action; that he has read the foregoing Petition for Authority to Institute Suit Against Bolsa Chica Oil Corporation, and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon information or belief, and as to those matters that he believes it to be true.

HUBERT F. LAUGHARN

Subscribed and sworn to before me this 20th day of September, 1940.

[Seal] MEREDITH KEITH

Notary Public in and for the County of Los Angeles, State of California. [44]

In the Superior Court of the State of California in and for the County of Los Angeles

No. .....

HUBERT F. LAUGHARN, as Trustee in Bankruptcy in the Matter of Jack Dave Sterling, Bankrupt,

Plaintiff,

vs.

BOLSA CHICA OIL CORPORATION, a corporation, ONE DOE, TWO DOE, THREE DOE, FOUR DOE, FIVE DOE COMPANY, a Corporation, and SIX DOE COMPANY, a corporation,

Defendants.

COMPLAINT FOR DAMAGES

Comes now the plaintiff and for the first cause of action against the defendants complains and alleges:

I.

That plaintiff is the duly elected, qualified and acting Trustee in Bankruptcy in the Matter of Jack Dave Sterling, Bankrupt, pending in the District Court of the United States, Southern District of California, Central Division, In Bankruptcy Consolidated Cause No. 26685-Y.

That said plaintiff was, pursuant to an order made and entered in said bankruptcy proceedings, authorized and empowered to institute, maintain and prosecute this action against said defendants.

II.

That the Bolsa Chica Oil Corporation is a corporation [45] organized and existing under and pursuant to the laws of the State of California with its principal office in the County of Los Angeles, within said state. That the defendants Five Doe Company and Six Doe Company are corporations organized and existing.

That the defendants One Doe, Two Doe, Three Doe, Four Doe, Five Doe Company, a corporation, and Six Doe Company, a corporation, are sued herein under fictitious names for the reason that the true names of said defendants are unknown to the plaintiff and plaintiff will ask leave of court to substitute the true names or said defendants when the same are ascertained.

III.

That Hubert F. Laugharn, as trustee in bankruptcy, was at all times hereinafter mentioned and now is the owner of that certain oil well commonly known as designated as the "Huntington Shore Well", drilled upon the real property in the County of Orange and State of California, more particularly described as follows:

> Lot Two (2) in Block Three Hundred Nineteen (319) of Huntington Beach Seventeenth Street Section in the City of Huntington Beach, as per Map recorded in Book 4, Page 10 of Miscellaneous Maps, Records of said County.

IV.

That the Bolsa Chica Oil Corporation was at all times herein mentioned the owner of and in charge of the redrilling operations upon that certain oil well commonly known and designated as "Petroleum Well", also sometimes known as "Fee No. 1 Well", drilled upon that certain real property situated in the County of Orange and State of California, more particularly described as follows:

> Lots Twenty (20) and Twenty-two (22) in Block One Hundred Nineteen (119) of the Huntington Beach Seventeenth Street Section in the City of Huntington Beach, as per Map recorded in Book 4, Page 10 of Miscellaneous Maps, records of said County. [46]

V.

That on or about the 15th day of April, 1940, the Bolsa Chica Oil Corporation commenced the redrilling of its said "Petroleum Well", also known as "Fee No. 1 Well", which was at that time and had for more than six months next preceding said date been off production. That as the direct and proximate result of the redrilling operations upon said "Petroleum Well", also known as "Fee No. 1 Well", carried on by the Bolsa Chica Oil Corporation mud, sand and other foreign substances infiltrated through the oil sands and were forced up and into the "Huntington Shore Well", owned by plaintiff. That as the direct and proximate result of a column of 3600 feet of mud, sand and other

foreign substances being forced up and into the "Huntington Shore Well" caused by the redrilling operations carried on by the Bolsa Chica Oil Corporation, plaintiff was compelled to and did shut down and suspend operations of the said "Huntington Shore Well" for a period of twenty (20) days from June 7, 1940 to June 27, 1940, while pulling, baling, cleaning, washing and other work was being carried on to remove the mud, sand and other foreign substances forced up and into said well.

VI.

That at the time of the commencement of said redrilling operations by the Bolsa Chica Oil Corporation the said "Huntington Shore Well" was producing 265 barrels of clean oil per day. That as the direct and proximate result of the infiltration and forcing of mud, sand and other foreign substances through the oil sands up and into the "Huntington Shore Well" caused by the redrilling operations of the Bolsa Chica Oil Corporation, when said "Huntington Shore Well" was again placed upon production on or about June 27, 1940, it produced 168 barrels of oil per day.

VII.

That the damage to plaintiff resulting from the loss of oil at 265 barrels per day computed at ninety (90) cents per barrel, which was the fair and reasonable market value of oil of said grade and [47] gravity in said field at said period and the

price which plaintiff would have received for said oil during said time, amounted to $4,770.00; that the damage to plaintiff as the result of twenty (20) days loss from wet and dry gas, computed upon the fair, reasonable and market value thereof and the price which plaintiff would have received therefor, amounted to $248.00; that the damage sustained by plaintiff for the period from June 27, 1940 to September 1, 1940, as the result of the decline of oil produced during said period computed upon the fair and reasonable market value thereof and the price plaintiff would have received therefor, amounted to 3700 barrels of oil at ninety (90) cents per barrel, or $3,330.00; that the damage sustained by plaintiff for the period from June 27, 1940 to September 1, 1940, as the result of the decline of proceeds from wet and dry gas amounted to $550.00; that the damage sustained to plaintiff on account of money expended and obligations incurred for pulling, baling, washing and other material, labor and technical assistance in the removal of the mud, sand and other foreign substances which had infiltrated and had been forced up and into said well amounted to $3,642.00, all to plaintiff's aggregate damage to September 1, 1940 of $12,540.00. That no part of said damages have been paid and the whole thereof is due, owing and unpaid.

VIII.

That in addition thereto, the production of oil and gas from said "Huntington Shore Well" has been

permanently and perpetually diminished and decreased for the balance of the life of said well to plaintiff's further damage in the sum of $250,000.00. That no part of said damage has been paid and the whole thereof is now due, owing and unpaid.

Comes now the plaintiff and for a second cause of action against defendants complains and alleges: [48]

I.

Plaintiff adopts Paragraphs I, II, III and IV. of his first cause of action as Paragraph I. of this, his second cause of action.

II.

That on or about the 15th day of April, 1940, the Bolsa Chica Oil Corporation commenced the redrilling of its said "Petroleum Well", also known as "Fee No. 1 Well", which was at that time and had for more than six months immediately preceding said date been off production. That as the direct and proximate result of the careless, negligent and unskillful operation, control and management of the Bolsa Chica Oil Corporation during the redrilling of said well, mud, sand and other foreign substances were forced through the oil sands up and into the "Huntington Shore Well". That as the direct and proximate result of the careless, negligent and unskillful operation, control and management of the Bolsa Chica Oil Corporation during the redrilling of said well, mud, sand and other

foreign substances were forced up and into said "Huntington Shore Well" forming a column 3600 feet high so that said "Huntington Shore Well" became mudded, sanded and clogged, resulting in the cessation of operations for a period of twenty (20) days from June 7, 1940 to June 27, 1940.

III.

That as the direct and proximate result of the careless, negligent and unskillful operation, management and control of the Bolsa Chica Oil Corporation, it was necessary for the plaintiff to pull, bale, wash, and incur other expeditures for material, labor and technical assistance in removing the mud, sand and other foreign substances from said "Huntington Shore Well" in order to restore said well to production. That as the direct and proximate result of the careless, negligent and unskillful operation, control and management of the Bolsa Chica Oil Corporation the plaintiff has sustained damages resulting from the loss of production oil and gas and remedial work in restoring the said "Huntington Shore Well" to September 1, 1940, [49] of $12,540.00. That no part of said damages has been paid and the whole thereof is now due, owing and unpaid.

IV.

That prior to the commencement of the redrilling operations by the Bolsa Chica Oil Corporation the said "Huntington Shore Well" was producing 265 barrels of clean oil per day and the proceeds from

wet and dry gas amounted to $328.00 per month. That as the direct and proximate result of the careless, negligent and unskillful operation, management and control of the Bolsa Chica Oil Corporation during such redrilling operations the production of oil from said "Huntington Shore Well", when said well was replaced upon production, had decreased to 168 barrels per day and the income of wet and dry gas had decreased to $154.00 per month. That as the direct and proximate result of said careless, negligent and unskillful operation, management and control of Bolsa Chica Oil Corporation during said redrilling operations the said "Huntington Shore Well" has become and is irreparably and permanently damaged in that the production of said "Huntington Shore Well" has been diminished and reduced and plaintiff has thereby sustained additional damages due to the loss of future production from said "Huntington Shore Well" to his further damage in the sum of $250,000.00. That no part of said damages has been paid to plaintiff and the whole is now due, owing and unpaid.

Wherefore, plaintiff prays judgment against the defendants for the sum of $262,540.00, together with the costs of suit incurred herein.

JOSEPH J. RIFKIND and
RAPHAEL DECHTER,
By JOSEPH J. RIFKIND,
Attorneys for Trustee in
Bankruptcy. [50]

State of California,
County of Los Angeles—ss.

Hubert F. Laugharn, being by me first duly sworn, deposes and says: that he is the Plaintiff in the above entitled action; that he has read the foregoing Complaint for Damages and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon information or belief, and as to those matters that he believes it to be true.

HUBERT F. LAUGHARN

Subscribed and sworn to before me this.....day of September, 1940.

.....

Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Petition for Authority to Institute Suit Against Bolsa Chica Oil Corporation—filed Sep. 20, 1940. Ernest R. Utley, Referee.

[Endorsed]: Filed Apr. 2-1941. R. S. Zimmerman, Clerk. [51]

[Title of District Court and Cause.]

ORDER AUTHORIZING SUIT AGAINST BOLSA CHICA OIL CORPORATION.

Upon reading the verified petition of Hubert F. Laugharn, the trustee in bankruptcy in the above entitled matter, for authority to institute suit

against the Bolsa Chica Oil Corporation for the recovery of damages sustained by the "Huntington Shore Well" owned and operated by the bankrupt estate as a result of the redrilling operations carried on by the Bolsa Chica Oil Corporation in connection with its "Petroleum Well", also known as "Fee No. 1 Well", at Huntington Beach, California, and good cause appearing therefor,

It Is Ordered that Hubert F. Laugharn, as trustee in bankruptcy in the above entitled matter, be and he is hereby authorized and empowered to institute, prosecute and maintain any action, proceeding or suit against the Bolsa Chica Oil Corporation which said trustee in bankruptcy may deem necessary, proper and advisable to recover from the Bolsa Chica Oil Corporation any and all damages sustained or which may hereafter be sustained to the "Huntington Shore Well" of said bankrupt estate as the result of the operations carried on by the Bolsa Chica Oil Corporation in connection with the redrilling of its "Petroleum Well", also known as "Fee No. 1 Well", at Huntington Beach, California.

It Is Further Ordered that Hubert F. Laugharn, as trustee in bankruptcy in the above entitled matter, be and he is hereby authorized and empowered to pay from the proceeds of said bankrupt [52] estate all of the costs, expenses and charges which may be incurred in connection with the institution, maintenance and prosecution of any such action which may be instituted, including any mo-

tion for a new trial or appeal which may be taken in connection therewith.

Dated this 20th day of September, 1940.

ERNEST R. UTLEY
Referee in Bankruptcy.

[Endorsed]: Filed Sep. 20, 1940, Ernest R. Utley, Referee.

[Endorsed]: Filed Apr. 2, 1941, R. S. Zimmerman, Clerk. [53]

[Title of District Court and Cause.]

CERTIFICATE OF CONTEMPT

The petition to have Bolsa Chica Oil Corporation, a corporation, McVicar-Rood, Inc., a corporation, M. M. McCallen Corporation (whose name was misspelled in the petition as M. M. McCullum Corporation), a corporation, H. H. McVicar, C. M. Rood, M. M. McCallen (whose name was misspelled in the petition as M. M. McCullum), Thomas W. Simmons, Allen A. Anderson (designated in the petition as "John Doe" Anderson), William S. Cree and Warren S. Pallette certified for contempt to the United States District Court for violating and aiding and abetting in the violation of that certain Injunction entered on May 15, 1940, in the above entitled matter, together with the Order to Show Cause issued thereon, and personally served upon each of said persons, came on regularly for hearing before the Honorable Ernest R. Utley, Referee in Bank-

ruptcy on August 30, 1940, at 10 o'clock A. M. and was on said date continued to September 26, 1940, at 10 o'clock A. M. and after being partially heard on said date was continued to September 30, 1940, and after being again partially heard on said date was continued to and concluded on October 1st, 1940. The petitioner, Hubert F. Laugharn, as Trustee in Bankruptcy, appeared through and was represented by Raphael Dechter and Joseph J. Rifkind, his attorneys; the respondents, Bolsa Chica Oil Corporation, a corporation, Thomas W. Simmons, Allen A. Anderson and Warren S. Pallette appeared at each of said hearings and were represented at each of said hearings by attorneys, Eugene Overton and Warren S. Pallette, of Overton, Lyman & Plumb, attorneys; the respondents [54] McVicar-Rood, Inc., a corporation, M. M. McCallen Corporation, H. H. McVicar, C. M. Rood, M. M. McCallen and William H. Cree appeared at each of said hearings and were represented at each of said hearings by attorneys William H. Cree and Elizabeth R. Henzel. Oral and documentary evidence having been introduced, the law applicable to the matter having been argued in open Court and by the filing of briefs by the respective counsel, the Court having been fully advised in the premises, now makes the following findings of fact, conclusions of law and certification to the United States District Court.

FINDINGS OF FACT

That Hubert F. Laugharn now is and at all times herein mentioned has been the duly appointed, qualified and acting trustee in bankruptcy in the above entitled matter. That one of the principal assets of said bankrupt estate is that certain oil well commonly known and designated as "Huntington Shore Well" situated in the County of Orange, State of California, on that certain real property more particularly described as follows:

> Lot Two (2) in Block Three Hundred Nineteen (319) of Huntington Beach Seventeenth Street Section in the City of Huntington Beach, as per map thereof recorded in Book 4, Page 10 of Miscellaneous Maps, Records of said County,

That said well is located in what is commonly known as the Huntington Beach Oil Field and said well was drilled and is being operated under an easement granted by the State of California, being Easement No. 309-2A.

That on or about the 20th day of September, 1936, the Termo Oil Company commenced the redrilling of its Termo Well and that as a result of said redrilling, sand, cement, and other foreign substances were forced through the oil sands up into the Huntington Shore Well, causing the equipment used in the operation of the Huntington Shore [55] Well to become clogged and stuck and making it impossible to operate or produce from said well. That as a result thereof the Trustee in Bankruptcy in an en-

deavor to clean out and remove the said sand, cement and other foreign substances, to dislodge and free the obstructions in said Huntington Shore Well expended on what is commonly known as a fishing job, the sum of approximately $20,000.00. That all efforts to free the equipment of said Huntington Shore Well proved unsuccessful and it was necessary for the Trustee in Bankruptcy to redrill said Huntington Shore Well at a cost of $80,000.00 and to surrender a 20% interest in said well in addition to said sum as part of the cost of redrilling said well. That said Huntington Shore Well after being redrilled was placed on production on August 15th, 1937, and the average daily production from said Huntington Shore Well since said date was 295 barrels per day.

That on or about April 15, 1940, the Bolsa Chica Oil Corporation commenced the redrilling of its well commonly known and designated as "Petroleum Well, also known as Fee No. 1 Well", situated in the County of Orange, State of California, on that certain real property more particularly described as follows:

> Lots Twenty (20) and Twenty-two (22) in Block One Hundred Nineteen (119) of the Huntington Beach Seventeenth Street Section in the City of Huntington Beach, as per Map recorded in Book 4, Page 10 of Miscellaneous Maps, records of said County,

That on said date the respondents were familiar with and were aware of the effect of the drilling of the Termo Well on the Huntington Shore Well.

That thereupon an application was made to the above entitled Court to enjoin the Bolsa Chica Oil Corporation from drilling its "Petroleum Well, also known as Fee No. 1 Well" at Huntington Beach, California, closer than 200 feet from the Huntington Shore Well and from using mud as a circulating fluid in the redrilling of said well. That [56] at said hearing testimony was introduced on behalf of the Trustee in Bankruptcy that if said well were drilled closer than 200 feet and if mud were used as a circulating fluid in the redrilling of said well that the mud so used in the said redrilling, which is pumped into the well in a liquid state under hydraulic pressure, would infiltrate and go through the oil sands carrying with it sand and other foreign substances which would clog up the oil sands and be forced up into the Huntington Shore Well and that in all probability serious and irreparable damage would result with a possible loss of said Huntington Shore Well. That after the testimony introduced on behalf of the trustee in bankruptcy and upon the conclusion of the cross-examination by the attorneys for the Bolsa Chica Oil Corporation of the witnesses called on behalf of the trustee in bankruptcy, the attorneys for the Bolsa Chica Oil Corporation stipulated in open court to the granting of an injunction against the Bolsa Chica Oil Corporation restraining them from coming closer than 200 feet from the Huntington Shore Well and prohibiting the Bolsa Chica Oil Corporation from using mud as a circu-

lating fluid in the redrilling of this well. That pursuant to the stipulation entered into between the attorneys for the trustee in bankruptcy and the attorneys for the Bolsa Chica Oil Corporation an injunction was submitted to the above entitled court which had been previously approved as to form and content by the attorneys for the trustee in bankruptcy and the attorneys for Bolsa Chica Oil Corporation, and said injunction was issued by the court on May 15, 1940. That notice of the entry of said injunction together with a copy of the injunction was served upon Overton, Lyman & Plumb as attorneys for the Bolsa Chica Oil Corporation, and also upon the Bolsa Chica Oil Corporation itself. That no petition for review or appeal has been taken from said injunction within the time provided by law, or otherwise, or at all, and the said injunction has become by operation of law final and absolute. [57]

That said injunction provides that the Bolsa Chica Oil Corporation, its superintendents, agents and employees shall be, and they are, restrained and enjoined from using any circulating fluid in the drilling, redrilling or side-tracking of said Petroleum Well, also known as Fee No. 1 Well, other than virgin crude oil maintained at a grade and gravity consistent with good oil field practice in said field and further provides that no mud, or other foreign substances of any kind, shall be used in lieu or as part of said circulating fluid unless mutually agreed to in writing by the petroleum engineers for

the respective parties thereto. That after the granting of said injunction and with full knowledge of the granting of the injunction and the terms thereof and after said injunction and the notice of the entry thereof had been served upon said Bolsa Chica Oil Corporation and its said attorneys, the said Bolsa Chica Oil Corporation resumed the redrilling of said Petroleum Well, also known as Fee No. 1 Well, by using mud as a circulating fluid in the redrilling thereof in direct violation of the express prohibition contained in said injunction against the use thereof.

That the petroleum engineer of the Trustee was aware of and had knowledge that the respondents were using mud on said Fee No. 1 Well, contrary to order of this Court, but said petroleum engineer of the Trustee had no supervision or control over the operations of respondents and said petroleum engineer of the Trustee did caution said respondents against using mud when they reached a depth of approximately 4025 feet, and if said warning of the petroleum engineer of the Trustee had been heeded, the damage resulting to the Trustee hereinafter set forth would not have occurred; that no consent in writing was ever given by the Trustee nor his engineer to the use of mud by the respondents; that it would have been good oil field practice when the respondents reached a depth of approximately 4,000 feet, to have commenced coring the formation through which the well of respondents was being drilled, and that if such cores had been taken they

would have indicated a formation [58] extending approximately over 200 feet containing streaks of oil sand, which would have indicated to respondents that they were approaching the main body of oil sand and which would have indicated to respondents the fact that to continue to use mud would mean that such mud would permeate and migrate through such sands to the well of the Trustee.

That as the result of the use of mud as a circulating fluid in the redrilling of said well, mud in liquid form, carrying with it sand and other foreign substances infiltrated through the oil sands and was forced up into the Huntington Shore Well, forming a column of mud in said Huntington Shore Well of 3700 feet from the bottom of said well. That as a result thereof, the production from and the operation of said Huntington Shore Well was shut down and suspended for a period of 20 days from June 7, 1940 to June 27, 1940, while pulling, baling, washing and other remedial work was being carried on on behalf of the Trustee in Bankruptcy in an endeavor to remove, clean out and dislodge the mud, sand and other foreign substances which had been infiltrated through the oil sands and forced up into said well as a result of the use of mud as a circulating fluid in said drilling operations. That said mud was brought on to the premises of the "Petroleum Well, also known as Fee No. 1 Well" and mixed into liquid form and in such liquid form forced into the well being redrilled under hydrostatic pressure; that

said mud escaped and was lost in said redrilling, and that it was received by and came up into the well of the Trustee in Bankruptcy; that specimens of the mud lost in the redrilling and received in the Huntington Shore Well were tested, analyzed and examined and shown conclusively to be the mud used in said redrilling.

That at the time of the commencement of said redrilling operations by the Bolsa Chica Oil Corporation, the Huntington Shore Well was producing 265 barrels of oil per day. That as the direct and proximate result of the infiltration and forcing of mud, sand and other foreign substances through the oil sands up and into the Huntington Shore Well [59] as the result of the redrilling operations of the Bolsa Chica Oil Corporation, the Huntington Shore Well, after being replaced upon production on or about June 27, 1940, produced 160 barrels of oil per day.

That the damage to the Trustee in Bankruptcy as the result of the use of mud as a circulating fluid in the redrilling of said well for the period of said 20 days was 265 barrels of oil per day at 90¢ per barrel, which was a fair and reasonable price of oil of said gravity in said field during said period and was the price that the Trustee would have received for oil produced during said period, amounting to $4,770.00. That the damage to the Trustee in Bankruptcy resulting from 20 days' loss of pressure from wet and dry gas at a fair and reasonable market price for wet and dry gas which the Trustee would

have received for such wet and dry gas amounts to $248.00. That the damage sustained by the Trustee as a result of the decline of oil produced during the period from June 27, 1940, to September 1, 1940, computed upon the fair and reasonable market value thereof and the price the Trustee would have received therefore, amounted to 3700 barrels of oil at 90¢ per barrel, or $3,330.00. That the damage sustained by the Trustee on account of money expended and obligations incurred for pulling, baling, washing and other remedial material, labor and technical assistance in the removal of the mud, sand and other foreign substances which had infiltrated through the oil sands and had been forced up into the said well, amounted to $3,642.00. All to the Trustee's aggregate damage as of September 1, 1940, in the sum of $12,540.00. That in addition thereto, the production of oil and gas from the Huntington Shore Well was shown to have been permanently impaired and decreased for the balance of the life of said well. That as the direct and proximate use of mud as the circulating fluid in the redrilling of said Petroleum Well, also known as Fee No. 1 Well, in violation of said injunction and the infiltration of said mud through the oil sands and up into the Huntington Shore Well, the production of said Huntington Shore Well has been diminished by approximately 60 barrels of [60] oil per day for the balance of the life of said well and that the reasonable life of said well is another ten years.

That the use of mud as a circulating fluid in the

redrilling operations were carried on by the Bolsa Chica Oil Corporation with the knowledge and consent and under the direction of Thomas W. Simmons, its president, and Allen A. Anderson, the superintendent in charge of redrilling operations, both of whom were familiar with the issuance and terms of said injunction of May 15, 1940.

That all of the damage sustained to and the impairment of the production from the Huntington Shore Well was anticipated by the Trustee in applying for said injunction and the purpose of issuing said injunction was expressly to avoid said consequences and such damage would not have resulted had mud not been used brought on to and used as a circulating fluid in the redrilling of said well. That such consequences were indicated and made known at the time of the application for and the granting of said injunction and said parties knew that such consequences would probably result from the use of mud as a circulating fluid, and nevertheless proceeded to use mud as a circulating fluid in open defiance and in violation of the express terms of the injunction.

That after said mud in liquid form carrying with it sand, debris and other foreign substances had infiltrated through the oil sands and had clogged and stopped up the Huntington Shore Well, further redrilling was suspended by the Bolsa Chica Oil Corporation on or about the 10th day of June, 1940.

That the attorneys for the Trustee in Bankruptcy upon obtaining information that the Bolsa Chica Oil

Corporation was about to resume the redrilling of said well with the use of mud as a circulating fluid sent a registered letter to the Bolsa Chica Oil Corporation on behalf of the Trustee in Bankruptcy, on July 31, 1940, again directing its attention to the injunction of this Court against the use of mud as a circulating fluid and again enclosing a copy of the injunction and notifying the [61] Bolsa Chica Oil Corporation that unless it forthwith desisted from using mud as a circulating fluid in the redrilling of said well that application would be made to the Court to have them cited for and certified for contempt for violating said injunction. That pursuant to said letter a conference was arranged by Thomas W. Simmons, president of Bolsa Chica Oil Corporation, on August 1st, 1940, at one o'clock P. M., at which there was present Thomas W. Simmons, president of Bolsa Chica Oil Corporation, Warren S. Pallette and William H. Cree, attorneys for said Bolsa Chica Oil Corporation, Mr. Allen A. Anderson, drilling superintendent of Bolsa Chica Oil Corporation, Vernon L. King, petroleum engineer for the Trustee in Bankruptcy, Mr. R. D. Holdredge, representing the Trustee, and Joseph J. Rifkind, one of the attorneys representing the Trustee. That the Bolsa Chica Oil Corporation, through its president, superintendent and attorneys requested and endeavored to procure an agreement or stipulation eliminating from the injunction the provision against the use of mud as a circulating fluid. That said Bolsa Chica Oil Corporation, through said

president on its behalf, was advised at said conference that as a result of the use of mud as a circulating fluid by the Bolsa Chica Oil Corporation that a column of mud 3700 feet high had been forced up into the Huntington Shore Well; that it had been necessary as a result thereof to shut down and suspend operations and to pull bale and wash said well in an endeavor to remove the mud and other obstructions from said well and that in addition to the loss and expense in so doing, the production from said well had been permanently impaired, that such condition was the best evidence that the use of mud as a circulating fluid was actually damaging the Huntington Shore Well and that no modification of the injunction in that respect would be stipulated to.

That Thomas W. Simmons, president of Bolsa Chica Oil Corporation stated at said conference that a large amount of money had been expended in the redrilling of said well and that mud was the only fluid [62] that could be used to advantage in the redrilling of said well and that some way would have to be found to resume redrilling operations despite said injunction. That William H. Cree, one of the attorneys for the Bolsa Chica Oil Corporation, at said conference, stated that he advised the ignoring of the injunction and the resumption of the redrilling of said well using mud as a circulating fluid, stating: "If this were my well I wouldn't pay any attention to the damned injunction." That counsel for the Trustee, at said conference, stated that the injunction was in full force and effect and until

said injunction was set aside or vacated by the Court or on review or on appeal, no other course would be open to the Trustee in the event said injunction was violated and mud used as a circulating fluid but to file a petition to have all of the offending parties cited for contempt of Court.

That previous to said conference Thomas W. Simmons, as President of Bolsa Chica Oil Corporation, had a conference with Raphael Dechter the other counsel for the Trustee, during the month of July, 1940, in which a proposal was made that if the Trustee would consent to the modification of the injunction permitting the use of mud as a circulating fluid instead of virgin crude oil that the Bolsa Chica Oil Corporation would be willing to assign to the Trustee a 25% interest in its well to commence participating after the costs of redrilling had been repaid. That prior to said conference Thomas W. Simmons as president of Bolsa Chica Oil Corporation also had a conference with J. D. Sterling in an endeavor to work out a modification of said injunction through him. That said injunction was not as a result of any of said conferences, or otherwise, or any time, or at all, in any manner whatsoever modified by consent of the parties on order of Court.

That information was thereafter received by the Trustee that an arrangement had been entered into by and between the Bolsa Chica Oil Corporation through Thomas W. Simmons, its president, and M. M. McCallen Corporation through H. H.

McVicar and C. M. Rood, its President [63] and Secretary, whereby the oil and gas lease of the Bolsa Chica Oil Corporation would be assigned to M. M. McCallen Corporation, which would resume said drilling operations. That upon receipt of said advice, a letter was sent by registered mail to McVicar-Rood, Inc., dated August 21, 1940, advising them of the injunction and the restriction against the use of mud in the redrilling thereof.

That William H. Cree was at all times herein mentioned and for many years last past has been the attorney for H. H. McVicar and C. M. Rood and was the attorney who organized and represented the M. M. McCallen Corporation, which is jointly and equally owned, controlled and managed by and is the corporate instrumentality of said H. H. McVicar and C. M. Rood; that said William H. Cree prepared the assignment of the oil and gas lease from the Bolsa Chica Oil Corporation to M. M. McCallen Corporation, dated August 14, 1940, and the drilling and operating agreement between Bolsa Chica Oil Corporation and M. M. McCallen Corporation, dated August 14, 1940; that said William H. Cree with full knowledge of said injunction, conducted the negotiations and prepared the agreement and assignment through which an attempt would be made to have it appear that M. M. McCallen Corporation, H. H. McVicar and C. M. Rood had succeeded to the rights of the Bolsa Chica Oil Corporation and had taken over the redrilling operations of said corporation. And all of said parties at the

time of said negotiations and the preparation and execution of said assignment knew that said agreement and assignment was for the purpose of misleading and deceiving the Court and not bona-fide or actual and was part of the conspiracy of said parties to violate the injunction of the Court aforesaid.

That Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, M. M. McCallen Corporation, H. H. McVicar, C. M. Rood and William H. Cree did at some time subsequent to August 1st, 1940, enter into a conspiracy for the purpose of violating and circumventing, and each of said parties aided and abetted the violation and circumvention [64] of said injunction and said assignment and agreement were colorable and not bona fide and were part of the subterfuge, scheme and device, deliberately, wilfully and premeditatedly planned and carried out under the belief and with the intent to evade and escape the force and effect of said injunction against the use of mud as a circulating fluid in the redrilling operation of the Petroleum Well, also known as Fee No. 1 Well. That disregarding the said injunction and the letters sent on behalf of the Trustee and the express admonition in that respect, the said parties commenced redrilling and again commenced the use of mud as a circulating fluid in the redrilling of said well on August 22, 1940. That the Trustee upon learning of the resumption of said redrilling operations and the use of mud as a circulating fluid in connection therewith filed a peti-

tion to have the Bolsa Chica Oil Corporation, et al., certified for contempt to the United States District Court and an order to show cause was issued on August 22, 1940, requiring said parties and each of them to show cause on August 30, 1940, at 10 o'clock A. M. why they should not be certified to the United States District Court for contempt for violating, aiding and abetting in the violation of the injunction of May 15, 1940, issued in the above entitled matter, and specifically restraining each of said persons from using mud as a circulating fluid pending the hearing of said order to show cause. That copies of said petition and the order to show cause issued thereon was served upon said parties on August 22, 1940, at 7 o'clock P. M.; that despite said order to show cause why said parties should not be cited for contempt of court they continued to use mud as a circulating fluid in the redrilling operations that entire night and through the following day.

CONCLUSIONS OF LAW

The Referee in Bankruptcy concludes that Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson are guilty of contempt of Court and said persons and each of them with full knowledge of said [65] injunction of May 15, 1940, resumed and permitted the resumption of the use of mud as a circulating fluid in the redrilling of said Petroleum Well, also known as Fee No. 1 Well; that the Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, M. M. McCallen Corpo-

ration, H. H. McVicar, C. M. Rood and William H. Cree are, and each of them is guilty in violating and aiding and abetting in the violation of the injunction of May 15, 1940, in using and permitting the use of mud as a circulating fluid when redrilling operations were resumed on August 22, 1940.

CERTIFICATE

The Referee in Bankruptcy therefore certifies the Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation and William H. Cree, and each of them, to the United States District Court for violating the injunction of May 15, 1940, issued in the above entitled matter, and for such punishment as the United States District Court may deem proper and appropriate for such contempt. The Referee in Bankruptcy further certifies that there are no extenuating or mitigating circumstances on behalf of said persons, or any of them, and that Bolsa Chica Oil Corporation, Thomas W. Simmons, its president, and Allen A. Anderson, its superintendent, is resuming redrilling subsequent to May 15, 1940, on the said Petroleum Well, also known as Fee No. 1 Well, used mud as a circulating fluid in direct violation of the express terms of the injunction and in the utter and open disregard thereof.

The referee in Bankruptcy finds no extenuating or mitigating circumstances on behalf of the second series of contempts occurring subsequent to August 1, 1940, but on the contrary that Bolsa Chica Oil

Corporation, Thomas W. Simmons, Allen A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation and William H. Cree did wilfully and premeditatedly plot and scheme and did enter into a conspiracy for the express and deliberate purpose of evading and circumventing the [66] injunction against the use of mud as a circulating fluid and knowing the damage likely to result from their conduct.

The Referee in Bankruptcy transmits herewith for the consideration of the United States District Court, the following:

1. Injunction against Bolsa Chica Oil Corporation, et al., dated May 15, 1940.

2. Petition to have Bolsa Chica Oil Corporation, et al., certified for contempt.

3. Order to Show Cause on Petition to have Bolsa Chica Oil Corporation, et al., certified for contempt, dated August 22, 1940.

4. Points and Authorities on behalf of the Trustee in Bankruptcy re Order to Show Cause why Bolsa Chica Oil Corporation, et al., should not be certified for contempt.

5. Points and Authorities on behalf of respondents Bolsa Chica Oil Corporation, Thomas W. Simmons and Allen A. Anderson re Order to Show Cause why they should not be certified for contempt.

6. Memorandum of Points and Authorities on behalf of respondents M. M. McCallen Corporation, H. H. McVicar, C. H. Rood and William H. Cree, re Order to Show Cause why they should not be certified for contempt.

7. Trustee's reply to Points and Authorities of respondents Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, M. M. McCallen Corporation, H. H. McVicar, C. M. Rood, and William H. Cree re Order to Show Cause in Contempt.

8. Summary by Trustee of loss and expense, dated September 26, 1940 introduced as Trustee's Exhibit No. 1.

9. Letter to Bolsa Chica Oil Corporation dated July 30, 1940, introduced as Trustee's Exhibit No. 2.

10. Drilling and Operating Agreement between Bolsa Chica Oil Corporation and M. *N*. McCallen Corporation dated August 14, 1940, introduced as Trustee's Exhibit No. 3. [67]

11. Assignment of Oil and Gas Lease from Bolsa Chica Oil Corporation to M. M. McCallen Corporation, dated August 14, 1940, introduced as Trustee's Exhibit No. 4.

12. Log offered for identification as Trustee's Exhibit No. 5.

13. Letter to McVicar-Rood, Inc., dated August 21, 1940, introduced as Trustee's Exhibit No. 6.

14. Reporter's transcript of April 26, and May 1st, 1940.

15. Reporter's transcript of September 26, September 30 and October 1st, 1940.

Dated: this 30 day of December, 1940.

ERNEST R. UTLEY,
Referee in Bankruptcy.

[Endorsed]: Filed Dec. 31, 1940. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [68]

[Title of District Court and Cause.]

MOTION OF BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLEN A. ANDERSON FOR AN ORDER TO SHOW CAUSE WHY A CERTIFICATE OF CONTEMPT SHOULD NOT BE DISMISSED.

Come Now Bolsa Chica Oil Corporation, a corporation, Thos. W. Simmons and Allen A. Anderson and move this court for an order directing George T. Goggin, Trustee of the above entitled bankrupt estate, and the Honorable Ernest R. Utley, Referee in Bankruptcy of this court, to appear on January 20, 1941 at 10:00 o'clock A. M., or as soon thereafter as counsel may be heard, and there and then to show cause why a certificate of contempt heretofore filed by the Honorable Ernest R. Utley on the 31st day of December, 1940 in the files and records of this court, should not be heard and dismissed. Said motion is made on the following grounds, to-wit:

1. A referee in bankruptcy and a federal district court have no jurisdiction to adjudge these movants to be in contempt, it appearing on the face of the record that said movants and each of them, did not consent to any of the proceedings herein.

2. A referee in bankruptcy and a federal district court have no jurisdiction or control over the property of third persons when said property is not an asset of the bankrupt estate or in the custody or control of said district court.

3. Said certificate of contempt is not supported by [69] the evidence.

4. The Referee wrongfully excluded material and competent testimony in said contempt proceedings before him.

Said motion will be based upon the affidavits of W. S. Pallette and Donald H. Ford attached hereto and made a part of this motion, upon the records and files of this proceeding and the memorandum of points and authorities attached hereto.

Signed: OVERTON, LYMAN & PLUMB
EUGENE OVERTON
W. S. PALLETTE
DONALD H. FORD
By DONALD H. FORD
Address: 733 Roosevelt Building,
727 West 7th Street,
Los Angeles, California. [70]

[Title of District Court and Cause.]

AFFIDAVIT OF W. S. PALLETTE

State of California,
County of Los Angeles—ss.

W. S. Pallette, being duly sworn, deposes and says:

That he is the Secretary of Bolsa Chica Oil Corporation, one of the defendants herein. That said Bolsa Chica Oil Corporation has expended in the redrilling of its Petroleum Fee #1 well at Huntington Beach, California the sum of approximately

$45,000.00, but that said well has not been completed. That in view of the injunction issued by the Referee in Bankruptcy herein and the petition for certification of contempt, Bolsa Chica Oil Corporation has been unable to conduct any work toward the completion of said well since prior to the 1st day of August, 1940. That said well is held under a certain Easement Agreement with the State of California, pursuant to which the operator of said well is entitled to produce oil from the tidelands lying offshore at Huntington Beach, California, into which tidelands said Petroleum Fee #1 well of Bolsa Chica Oil Corporation and the well belonging to the Trustee for the bankrupt, are drilled.

That the lease under which Bolsa Chica Oil Corporation is entitled to the use of the land upon which the surface location of the well is located, will shortly expire, in which event Bolsa Chica Oil Corporation will no longer have any right, title or interest in said well and will be unable to complete or pro- [71] duce the same. That the State of California, through representatives of the State Lands Commission, having jurisdiction over the Easement Agreement under which said well may be produced from the state-owned tidelands, has threatened to rescind and revoke, cancel and terminate said Easement Agreement for failure to produce said well, unless drilling operations are forthwith re-commenced. That it is therefore necessary that an immediate determination of the validity of the

Referee's order of injunction by the United States District Court be obtained, inasmuch as if it is determined that the Referee was without jurisdiction to make such order, Bolsa Chica Oil Corporation will then be in a position to make the necessary arrangements with the State of California for the completion of said well and thereupon complete the same, with the opportunity of recouping its expenditures to date of approximately $45,000.00 in connection with the redrilling of said well. That it is to the advantage of the Trustee in Bankruptcy that these proceedings be postponed, inasmuch as failure to obtain an immediate determination will result in the loss of this valuable property by Bolsa Chica Oil Corporation for the reasons above set forth, and that affiant believes that the Trustee in Bankruptcy will take no steps toward bringing this matter on for hearing immediately.

W. S. PALLETTE

Subscribed and Sworn to before me this 9th day of January, 1941.

[Seal] M. DE VINEY

Notary Public in and for the County of Los Angeles, State of California.

My Commission Expires March 2, 1943. [72]

[Title of District Court and Cause.]

AFFIDAVIT OF DONALD H. FORD

State of California,
County of Los Angeles—ss.

Donald H. Ford, being duly sworn, deposes and says:

That he is an attorney-at-law duly admitted to practice before the United States District Court, Southern District of California, Central Division. That he is one of the attorneys for defendants herein, Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson. That he has made an examination of the files and records in the above entitled proceeding. That nothing appears of record in said proceeding since the filing of the Certificate of Contempt against said defendants and others on December 31st, 1940, by the Honorable Ernest R. Utley, Referee in Bankruptcy, with reference to bringing said Certificate of Contempt on for hearing before the Court. That an examination of the Certificate of Contempt and the matters incorporated therein by reference reveals that while the Certificate of Contempt on its face shows that these defendants consented to the jurisdiction of the Referee to entertain the proceeding involved and to issue the order of injunction therein, the order of injunction and the transcripts of the proceedings show on their faces that these defendants at all times objected to and maintained their objections to the jurisdiction of the Referee to entertain said pro-

ceedings or to make and enter said order. That affiant believes that said [73] order was beyond the jurisdiction of the Referee in Bankruptcy to make by summary proceeding in the absence of a plenary suit. That on the face of the record neither the Referee in Bankruptcy nor this Honorable Court has jurisdiction to make or enter said order in the absence of consent of said defendants. That any damage which the trustee in bankruptcy may have suffered is fully ascertainable and recoverable in an action for damages in the proper tribunal. That the trustee in bankruptcy has commenced an action in the Superior Court of the State of California, in and for the County of Los Angeles, being number 456167 in said Court for the purpose of recovering damages on account of the alleged actions of these defendants, which said action is now pending in said Court and which said action was filed on or about the 20th day of September, 1940.

DONALD H. FORD

Subscribed and sworn to before me this 9th day of January, 1941.

[Seal] M. DE VINEY,
Notary Public in and for said County and State.

My Commission Expires March 2, 1943.

[Endorsed]: Motion for Order to Show Cause. Filed Jan. 9, 1941. [74]

[Title of District Court and Cause.]

ORDER TO SHOW CAUSE ON MOTION OF BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLEN A. ANDERSON RELATIVE TO CERTIFICATE OF CONTEMPT.

Upon reading and filing the motion of Bolsa Chica Oil Corporation, Thos. W. Simmons and Allen A. Anderson in the above entitled matter, together with the affidavits of W. S. Pallette and Donald H. Ford, and good cause appearing therefrom,

It Is Ordered that George T. Goggin, Trustee of the above entitled bankrupt estate, and the Honorable Ernest R. Utley, Referee in Bankruptcy of this court, be and appear before the Honorable Leon R. Yankwich in Court Room No. 5, Federal Building, Temple and Spring Streets, Los Angeles, California on the 27th day of January, 1941 at 10:00 o'clock A. M., then and there to show cause, if any they have, why the certificate of contempt heretofore filed on December 31, 1940 in the files and records of the above entitled proceeding should not be dismissed.

It Is Further Ordered by the above entitled court that a copy of the motion of Bolsa Chica Oil Corporation, Thos W. Simmons and Allen A. Anderson and the affidavits of W. S. Pallette and Donald H. Ford be served concurrently with the service of this order.

Dated: January 9, 1941.

PAUL J. McCORMICK, Judge.

[Endorsed]: Filed Jan. 9, 1941. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [75]

[Title of District Court and Cause.]

ORDER TO SHOW CAUSE IN RE CONTEMPT AGAINST BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLEN A. ANDERSON, ET AL.

It appearing to the Honorable Ernest R. Utley, Referee in Bankruptcy that Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation and William H. Cree, and each of them, be adjudged in contempt, and the Honorable Ernest R. Utley, Referee in Bankruptcy, having certified the facts to the Honorable Paul J. McCormick, United States District Judge, now, therefore,

It Is Ordered that Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation and William H. Cree, and each of them, are hereby directed to appear in the Courtroom of the Honorable Paul J. McCormick, United States District Judge, in the Federal Building, Los Angeles, California, on Monday, the 20th day of January, 1941, at the hour of 10 o'clock A. M., and then and there show cause if any they or any of them may have, why an order should not be made adjudging them, and each of them, as being in contempt.

It Is Further Ordered that service of this order to show cause may be made on counsel of record who

have heretofore appeared for said persons above named before this Court.

Dated this 13 day of January, 1941.

ERNEST R. UTLEY,
Referee in Bankruptcy.

[Endorsed]: Filed Jan. 14, 1941. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [76]

At a stated term, to wit: The September Term, A. D. 1940, of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles, California, on Thursday the 30th day of January in the year of our Lord one thousand nine hundred and forty-one.

Present: The Honorable Leon R. Yankwich,
District Judge.

No. 26,685-Y Bkcy.

In the Matter of

JACK DAVE STERLING,
Bankrupt.

This matter coming before the Court for (1) further hearing on return of order of February 9, 1941, to George T. Goggin, Trustee, to show cause why the certificate of contempt filed Dec. 31, 1941, should

not be dismissed; (2) hearing on return of order of January 13, 1941, to Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation, and W. H. Cree to show cause why they should not be adjudged in contempt pursuant to the certificate of the referee; Raphael Dechter and J. J. Rifkind, Esqs., appearing as counsel for the Trustee; Elizabeth Hensel, Attorney, appearing as counsel for Respondent Cree, et al.; Eugene Overton and W. S. Pallette, Esqs., being present for movants and respondents Bolsa Chica Oil Corporation; and G. M. Fox, Court Reporter, being present and reporting the testimony and the proceedings:

The Court makes a statement; Attorney Dechter argues further for the Trustee; Attorney Pallette argues further for the respondent; Attorney Rifkind argues further for the Trustee; and Attorney Hensel argues for Respondent Cree. Court recesses to 2 o'clock P. M.

At 2 o'clock P. M. court reconvenes, and all being present as before, Attorney Dechter argues further for the Trustee. [77]

The Court comments on facts, record and authorities. The Clerk is ordered to make petition and order part of the record in this proceeding.

The Court sustains objection to the jurisdiction and declines to hear further upon the certificate of contempt.

Attorney Dechter asks that injunction remain in effect.

Counsel for prevailing parties will prepare formal order. Meanwhile, injunction shall remain in effect. [78]

In the District Court of the United States
Southern District of California
Central Division

In Bankruptcy Consolidated Cause No. 26685-Y

In the Matter of

JACK DAVE STERLING,

Bankrupt.

ORDER

Re: Certificate of Contempt

This cause came on to be heard on Monday, January 20, 1941, and was continued to Monday, January 27, 1941, before the Honorable Leon R. Yankwich, Judge of the above entitled Court, on Order to Show Cause made by the Honorable Paul J. McCormick, Judge of said Court, on January 9, 1941, on Motion of Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson, relative to Certificate of Contempt filed by the Honorable Ernest R. Utley, Referee in Bankruptcy, in said Court, on December 31, 1940, and on Order to Show Cause in re Contempt against Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson, et al., made by said Honorable Ernest R. Utley, Referee in Bankruptcy, on January 13, 1941, and on said Certificate of Contempt and the pleadings and

records referred to therein. Said cause, after being partially heard on said January 27, 1941, was continued to January 30, 1941, for further hearing, and was further heard and concluded on said day. The Trustee in Bankruptcy, George T. Goggin, appeared through and was represented by Joseph J. Rifkind and Raphael Dechter, his attorneys; Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson appeared specially through and were represented by Overton, Lyman & Plumb, Eugene Overton and W. S. Pallette, their attorneys; and William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation appeared specially through and were represented by Elizabeth R. Hensel and William H. Cree, their attorneys. [79]

Said Bolsa Chica Oil Corporation, Thos. W. Simmons, Allan A. Anderson and William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation, through their respective attorneys, at the commencement of the hearing, stated to the Court that each of them was appearing specially for the sole purpose of objecting to any jurisdiction of the District Court or the Referee in Bankruptcy to hear or determine the issues involved in this cause.

The Court considered said Certificate of Contempt and the pleadings and record supporting the same and heard argument of counsel in connection therewith. From such consideration and argument it appeared to the Court that the Referee in Bankruptcy and this United States District Court, and each of

them, were at all times in this cause involved and now are without jurisdiction to make or enter the Injunction upon which said Certificate of Contempt is based. The Court being fully advised in the premises, refused to hear any evidence upon or determine the merits of the controversy, and thereupon

Ordered, Adjudged and Decreed As follows:

1. That the objections of Bolsa Chica Oil Corporation, Thos. W. Simmons, Allan A. Anderson, William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation, and each of them, to the jurisdiction of the Referee in Bankruptcy and this Court, and each of them, to make or enter said Injunction or to hear or determine the issues presented by said Certificate of Contempt and the pleadings and record in this proceeding are hereby sustained, and the Certificate of Contempt filed by the Referee in Bankruptcy in this cause on December 31, 1940, is hereby dismissed.

Dated this 7th day of February, 1941.

LEON R. YANKWICH,
Judge of the above entitled Court. [80]

Approved As to Form:

JOSEPH J. RIFKIND and
RAPHAEL DECHTER,
By R. DECHTER
Attorneys for Trustee
OVERTON, LYMAN & PLUMB,
EUGENE OVERTON and
W. S. PALLETTE
By W. S. PALLETTE
Attorneys for Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson
ELIZABETH R. HENSEL and
WILLIAM H. CREE
By.....
Attorneys for William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation.

[Endorsed]: Filed Feb. 7, 1941. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [81]

[Title of Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that George T. Goggin, Trustee in Bankruptcy of the above entitled bankrupt estate, hereby appeals to the Circuit Court of Appeals for the Ninth Circuit from the order dismissing the Referee's Certificate citing Bolsa Chica

Oil Corporation, a corporation, M. M. McCallen Corporation, a corporation, H. H. McVicar, C. M. Rood, Thos. W. Simmons, Allan A. Anderson and William H. Cree, to the District Court for contempt, the minute order of which was entered in this proceeding on the 30th day of January, 1941, and the formal order of dismissal being entered in this proceeding on the 7th day of February, 1941.

Dated this 13th day of February, 1941.

RAPHAEL DECHTER and
JOSEPH J. RIFKIND
By R. DECHTER
Attorneys for Trustee

[Endorsed]: Filed Feb. 13, 1941. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk [82]

[Title of District Court and Cause.]

No. 26685-Y

DIRECTIONS TO CLERK OF DISTRICT COURT FOR A NOTIFICATION OF FILING OF NOTICE OF APPEAL AND MAILING COPIES THEREOF TO ALL PARTIES TO THE JUDGMENT OTHER THAN THE PARTY TAKING THE APPEAL.

To R. S. Zimmerman, Clerk of the above entitled Court:

Pursuant to the provisions of Rule 73(b) of the New Rules of Civil Procedure, you are hereby noti-

fied to give Notice by Mail of the filing of the appeal to the following parties to the judgment, other than the party taking this appeal, or to their counsel of record, as follows:

Name of Party	Name of Counsel, and Address
Bolsa Chica Oil Corporation, Thos. W. Simmons, and Allan A. Anderson	Overton, Lyman & Plumb, Eugene Overton and W. S. Pallette, 733 Roosevelt Bldg. Los Angeles, Calif.
William H. Cree, H. H. McVicar, C. M. Rood, and M. M. McCallen	Elizabeth R. Hensel and William H. Cree 410 Park Central Bldg. Los Angeles, Calif.
Corporation	

Dated: This 13th day of February, 1941.

R. DECHTER

Attorney for Appellant.

Mailed to above counsel, 2/13/41. E. L. S.

[Endorsed]: Filed Feb. 13, 1941. R. S. Zimmerman, Clerk. By C. A. Simmons, Deputy Clerk. [83]

[Title of District Court and Cause.]

ORDER EXTENDING TIME TO DOCKET APPEAL

Good cause appearing therefor,

It is hereby ordered that the time to docket the appeal in the above entitled matter, is hereby extended to April 15th, 1941.

Dated this 25th day of March, 1941.

LEON R. YANKWICH
Judge of the District Court.

[Endorsed]: Filed Mar. 25, 1941, R. S. Zimmerman, Clerk. [94]

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, R. S. Zimmerman, Clerk of the United States District Court for the Southern District of California, do hereby certify that the foregoing pages, numbered 1 to 105, inclusive, contain full, true and correct copies of the Debtor's Petition under Section 74 of the Bankruptcy Act; Order Approving Debtor's Petition; Debtor's Petition for Adjudication; Adjudication and Order of Reference; Order of Re-Reference; Appointment of Hubert F. Laugharn as Trustee; Order Approving Bond of Trustee Hubert F. Laugharn; Resignation of Trustee Hubert F. Laugharn; Appointment of George Goggin as Trustee; Order Approving Bond of Trustee

George Goggin; Petition of Trustee for Instructions; Affidavit of Vernon L. King; Affidavit of Jack Dave Sterling; Order to Show Cause on Petition for Instructions; Injunction Against Bolsa Chica Oil Corporation, et al.; Petition to Have Bolsa Chica Oil Corporation, et al., Certified for Contempt; Order to Show Cause on Petition to Have Bolsa Chica Oil Corporation, et al., Certified for Contempt; Petition for Authority to Sue Bolsa Chica Oil Corporation, and Proposed Complaint attached thereto; Order Authorizing Suit Against Bolsa Chica Oil Corporation; Certificate of Contempt; Motion to Dismiss Certificate of Contempt; Affidavit of W. S. Pallette; Affidavit of Donald H. Ford; Order to Show Cause on Motion to Dismiss Certificate of Contempt; Order to Show Cause on Certificate of Contempt; Minute Order Granting Motion to Dismiss Certificate of Contempt; Order Dismissing Certificate of Contempt; Notice of Appeal; Service of Notice of Appeal; Statement of Points Upon Which Appellant Intends to Rely on Appeal; Appellant's Designation of Contents of Record on Appeal; Appellee's Designation of Contents of Record on Appeal; Appellant's Supplemental Designation of Contents of Record on Appeal; Order Extending Time to Docket Cause on Appeal; Order for [106] Transmittal of Original Exhibits on Appeal; Trustee's Exhibits Nos. 1, 3 and 4 (filed by Referee on Sept. 26, 1940); which, together with the originals of three volumes of Reporter's Transcript, and the originals of Trustee's

Exhibits 1 to 5, inclusive, (filed by Referee April 26, 1940), transmitted herewith, constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I do further certify that the Clerk's fee for comparing, correcting and certifying the foregoing record is $21.20, which fee has been paid to me by the Appellant.

Witness my hand and the seal of said District Court, this 11th day of April, A. D. 1941.

[Seal] R. S. ZIMMERMAN,
Clerk.
By EDMUND L. SMITH,
Deputy Clerk. [107]

[Title of District Court and Cause.]

REPORTER'S TRANSCRIPT OF PROCEEDINGS IN RE: ORDER TO SHOW CAUSE RE: PETITION FOR INSTRUCTIONS.

Los Angeles, California.
Friday, April 26, 1940
Wednesday, May 1, 1940.

Appearances:

Joseph J. Rifkind, Esq. and
Raphael Dechter, Esq.,
for the Trustee.
C. A. Borden, Esq. and
Warren S. Pallette, Esq.,
for Bolsa Chica Oil Corporation.

The Referee: Are you ready to proceed in the Sterling matter?

Mr. Rifkind: Yes, your Honor.

The Referee: You may proceed.

Mr. Rifkind: Mr. King, will you please take the stand?

Mr. Borden: At this time I would like to say we are here in obedience to the order to show cause. I am representing the Bolsa Chica Oil Corporation. While, of course, we concede your Honor's authority to make any orders you may deem necessary with respect to directing the Trustee in his work, we do not concede any jurisdiction to make any order that would affect us in this proceeding, we not being a party to the proceeding, but are appearing only specially here and are not submitting to the jurisdiction of the Court.

The Referee: You are objecting to the jurisdiction of the Court to make any orders affecting your company?

Mr. Borden: Yes, your Honor.

Mr. Dechter: May it please the Court, even if that objection was well-founded this Court must necessarily receive evidence to be able to rule on that objection. In other words, it must receive sufficient evidence to determine whether or not the Court has summary jurisdiction.

The Referee: Yes, I think that is true. [108]

Mr. Dechter: We contend this Court would

have summary jurisdiction to make an order binding on the Bolsa Chica Oil Corporation. First, the property is in the property involved and in the control of the bankruptcy court, and the property so in the possession of the bankruptcy court is, by the allegations in the petition and by the proof we expect to put on, is about to be threatened so as to be destroyed almost completely by the actions of the Bolsa Chica Oil Corporation. Also, the bankruptcy court not only has the right to protect this property, but also has the power to enforce orders made by this Court. One of the orders heretofore made by this Court was an order to place this well under production and to maintain and operate the same. It is our position that if our proof is as we expect it to show, that the Trustee in this case has a situation analogous to a Trustee operating a department store, and would be like someone coming into the department store day in and day out removing the property of the bankruptcy court. We think that situation is analogous and we expect our proof to so show.

Mr. Borden: If there was any such analogy we would agree to it.

The Referee: Well, let me swear the witness.

(Witness sworn).

The Referee: Well, I think gentlemen I have studied this petition, and as I understand

it the Sterling estate has a certain oil well. This petition alleges this company is [109] contemplating drilling a well in such a way as might interfere with the well of the bankrupt estate. I don't think this court would have any jurisdiction to prevent this company or any other company from drilling a well, but if it interfered or threatened to interfere with the bankrupt's property in any way, I think to that extent the Court would have jurisdiction.

Mr. Borden: Under the very allegations of the petition, your Honor, it does not appear we are in any way trespassing upon the property of the bankrupt. In other words, we are drilling from our own drill-site. We are not trespassing on their property according to the very allegations of the petition.

I am not here to offer any objection or demurrer because we are appearing here objecting to the jurisdiction of the Court.

The Referee: Your objection may appear; however, the Court must examine in a preliminary way this matter in order to determine whether or not it does have jurisdiction.

Mr. Borden: I appreciate that, your Honor.

The Referee: Very well, you may proceed.

TRUSTEE'S EXHIBIT NO. 1

Regulation Governing Redrilling Operations of Wells Drilled in Lands of the State of California.

No permit or consent for redrilling existing oil and gas wells will be granted unless the following conditions can be met:

(1) No point in the redrilled portion of the well shall be farther than 100 feet from the old hole. That is to say, the redrilled hole shall be restricted to a cylinder of 100 feet radius with the old hole as the axis of said cylinder.

(2) The bottom of the redrilled hole shall be located not more than 100 feet from the bottom of the old hole.

(3) No part of the redrilled hole not open to production (blanked off) shall come closer than 50 feet from any existing well other than the abandoned well being redrilled.

(4) No part of the redrilled hole open to production (perforated) shall come closer than 200 feet from the perforated portion of any existing well other than the abandoned well being redrilled.

(5) All drilling within the oil zone shall be done with oil as circulating fluid.

(6) No applications for redrilling will be considered unless it is shown that the proposed redrilling is necessary or desirable because of the poor mechanical condition of the old well.

The undersigned Executive Officer of the State Lands Commission does hereby certify the foregoing to be a true and correct copy of a "Regulation Governing Redrilling Operations of Wells Drilled in Lands of the State of California" duly promulgated by the State Lands Commission at a meeting held in the office of the Director of Finance, State Capitol, Sacramento, December 30, 1938, and that said regulation has not been amended or repealed.

WEBB SHADLE
Executive Officer,
State Lands Commission.

Los Angeles
April 26, 1940.

[Endorsed]: Tr. Exhibit No. 1. Filed Apr. 26, 1940. Ernest R. Utley, M. K.. Referee.

[Endorsed]: Filed Mar 28 1941 R. S. Zimmerman, Clerk. [110]

Mr. Dechter: All right, you may take the witness.

The Referee: Do you want to cross examine the witness?

Mr. Borden: I do, your Honor, without waiving my objection to jurisdiction.

The Referee: Very well. [130]

TRUSTEE'S EXHIBIT NO. 2

Huntington Shore Oil Company
State of California
Department of Finance
Division of State Lands
State Capitol
Sacramento

Agreement for Easement No. 309
Huntington Beach

This Agreement made and entered into this 1st day of March, 1934, by and between the State of California, through the duly appointed, qualified and acting Director of Finance of the State of California, and the duly appointed, qualified and acting Chief of the Division of State Lands of the Department of Finance, State of California, party of the first part, hereinafter called the State, and Jennie B. Durkee, Elizabeth Decker, Edna J. Decker, John R. Johnson and Vera Johnson, husband and wife, Rosa L. Boyd, John T. Kearns and Frances E. Kearns, husband and wife, Jasper N. Chamberlain and Amy Chamberlain, husband and wife, Lewis Pendleton and Mattie Pendleton, husband and wife, Vincent C. Croal, Mary J. Croal, F. H. Rolapp, Receiver of Sunset Pacific Oil Company, a corporation, Sunset Pacific Oil Company, a corporation, Fannie E. Finley, Nathan Nash, Dr. Fred M. Binkley and Mary Belle Binkley, husband and wife, Iona S. Sharp, Nellie P. Mooers, Tide Petroleum Company, a California corporation, Irene Abel, a married woman, John C. Gardiner,

Jacob E. Miller and Virginia Miller, Celestine R. Young, Bertha L. Gregory, J. J. Thompson and M. J. Thompson, John Kniss and Thelma A. Kniss, Sovereign Oil Corporation, a Nevada corporation sometimes erroneously referred to as Sovereign Oil Company, Charles M. Box and John W. Topham, Arvilla Decker, Chas. S. Chaffee and Zaidee M. Chaffee, Huntington Shore Oil Company, Nellie G. Pendleton, William Hazlett, as Trustee for Huntington Shore Oil Company, parties of the second part, hereinafter sometimes called the Grantee, pursuant to the provisions of Chapter 593, Statutes of California, 1933, Sections 654 and 675 of the Political Code, Chapter 402, Statutes of California, 1931, as amended, Chapter 303, Statutes of California, 1921, as amended, and such other statutes as are applicable, and to any and all implied powers of the State of California to compromise litigation, all of which said statutory references are hereinafter referred to as The Act:

Recital

The State of California is the owner in its sovereign and proprietary capacities of certain lands situated in the County of Orange, State of California, hereinafter more particularly described, containing quantities of oil, gas, and other petroleum products; that adjacent to a portion of said lands so owned by the State of California and containing said oil and gas and other petroleum products is the Seventeenth Street Addition to the City

of Huntington Beach, County of Orange, State of California; that upon said Seventeenth Street Addition to the City of Huntington Beach One (1) oil well, commonly known as No. 2, have been drilled by Huntington Short Oil Company, a California corporation, upon real property owned in fee simple by said Jennie B. Durkee, Elizabeth Decker, Edna J. Decker, John R. Johnson, Vera Johnson, Rosa L. Boyd, John T. Kearns, Jasper N. Chamberlain, Amy Chamberlain, Lewis Pendleton and Mattie Pendleton, Vincent C. Croal and Mary J. Croal, F. H. Rolapp, Receiver of Sunset Pacific Oil Company, a corporation, Sunset Pacific Oil Company, a corporation, Fannie E. Finley, Nathan Nash, Dr. Fred M. Binkley and Mary Belle Binkley, Iona S. Sharp, Nellie P. Mooers, and Nellie G. Pendleton, that said oil wells were drilled in such manner as to cause the same to cross lands intervening between the said Seventeenth Street Addition to the City of Huntington Beach and the ordinary high-water mark of the Pacific Ocean and to enter in, upon, and under the said lands of the State of California, to which reference is hereinbefore made, and to enter the oil, gas and/or petroleum deposits thereof, and the bottoms of said wells, and portions of said wells, are now through, in and under said lands of the State of California, and that said wells have drained, taken, and received and are capable of draining, taking and receiving oil, gas, and other petroleum products from the oil and gas deposits of said lands of the State of California; the Grantee

is willing to compensate the State of California for all oil, gas and other petroleum products heretofore drained, taken, and received from said lands of the State of California by means of the said wells known as No. 2 and the State is willing to enter into an agreement with the Grantee whereby compensation may be had for all such oil, gas and other petroleum products produced through the said wells, and to permit the Grantee to continue to take oil, gas and other petroleum products from said lands of the State of California, through said oil wells known as No. 2 and subject to the terms, covenants and conditions hereinafter set forth. The said lands belonging to the Grantee and the said lands belonging to the State of California, to which references are hereinbefore made, are more particularly hereinafter described,

Now, Therefore, Witnesseth:

Section 1. That the State, in consideration of the royalties to be paid and the covenants to be observed as herein set forth, does hereby grant to the Grantee easements appurtenant to said lands of Grantee first hereinafter described, through, in and under the said lands belonging to the State of California hereinafter more particularly described (which said easements are more particularly hereinafter described), and the right to drain, take, receive, extract, remove, produce and use oil, gas, and other petroleum products, through those certain oil wells commonly known and designated as No. 2 respectively, the tops of which said wells are located

upon those certain lands of Grantee situated in the County of Orange, State of California, and more particularly described as follows, to-wit:

> Lots Two (2) in Block Three Hundred Nineteen (319) of "Huntington Beach, Seventeenth St. Section", as shown on a Map recorded in Book 4, page 10 of Miscellaneous Maps, records of Orange County, California,

and through any other wells which may hereafter be drilled upon said property with the consent, in writing, of the Chief of the Division of State Lands being first had and obtained, and subject to the terms, covenants, and conditions herein contained, in so far as applicable, and otherwise in accordance with rules and regulations of the Division of State Lands now promulgated, and such reasonable rules and regulations of said Division of State Lands as may be promulgated hereafter from those certain lands in the Pacific Ocean belonging to the State of California situated in the County of Orange, more particularly described as follows:

> Beginning at a point in the ordinary high water mark of the Pacific Ocean where the North-South quarter section line of Section 4 T. 6 S., R. 11 W., S. B. B. M., projected in a straight line southerly, intersects said ordinary high water mark; thence southeasterly along said ordinary high water mark a distance of three (3) miles to a point in said ordinary high water mark; thence southwesterly at right an-

gles with said ordinary high water mark and in a straight line three (3) miles from said ordinary high water mark to a point in the Pacific Ocean; thence northwesterly along a line which is parallel to said ordinary high water mark a distance of three (3) miles to a point in the Pacific Ocean; thence northeasterly in a straight line to the point of beginning, (hereinafter sometimes referred to as said lands of the State of California);

for a period of twenty (20) years from the date hereof, with the preferential right in the Grantee to renew this agreement for successive periods of ten (10) years each, upon such reasonable terms and conditions as may be prescribed by the State, acting through the Chief of the Division of State Lands, hereinafter sometimes referred to as the Chief, unless otherwise provided by law at the time of the expiration of such periods.

Section 2. In consideration of the foregoing, the Grantee hereby agrees:

(a) To furnish a corporate surety bond, approved by the Chief, in the penal sum of two thousands (2,000) dollars, for each easement herein granted, conditioned upon compliance with the terms, conditions and covenants of this agreement.

(b) To pay to the State of California a royalty in accordance with the formula and schedule marked Exhibit "A", attached hereto, and by reference made a part hereof, on the oil produced, drained,

and saved from the said lands of the State of California hereinbefore described, or on demand of the State, acting through the Chief, a percentage of the oil produced in accordance with said Exhibit "A", the royalty when paid in value to be due and payable monthly not later than the 25th of each calendar month following the calendar month in which produced; and when paid in kind, to be delivered in the field and taken by the State at the receiving tanks of the Grantee on twenty-four (24) hours notice of the Grantee that a tankful of oil is ready for delivery; to pay to the State of California at the times and in the manner herein specified for the payment of royalty on oil, one-fifth (1/5) of the net proceeds received by the Grantee upon all gas, whether dry or wet, and upon all casinghead gasoline, produced and sold. Unless such gas or casinghead gasoline is sold pursuant to a sales-contract approved by the Chief, the price shall be the reasonable market price as fixed by the Chief. In case the gas produced and sold has a value both for casinghead gasoline content and as a dry gas from which the casinghead gasoline has been extracted, then the royalty above provided shall be paid upon the proceeds of each of such values.

The State may take its royalty dry gas in kind at its option, delivery thereof to be made at the casinghead manufacturing plant where produced, or at such other place as the parties hereto may agree.

(c) To file with the Division of State Lands of the Department of Finance true and correct copies of all sales-contracts for the disposition of oil, gas and other petroleum products produced hereunder, and in the event the State, acting through the Chief, shall elect to take such oil or gas royalty in money instead of oil or gas, not to sell or otherwise dispose of the oil or gas produced hereunder, except in accordance with such sales-contracts or other method first approved in writing by the State, acting through the Chief.

(d) To furnish monthly statements in detail in such form as may be prescribed by the State, acting through the Chief, showing, with respect to said wells, the amount, gravity, quality, and value of all oil produced, saved and/or sold, the amount of gas produced, saved, and sold and the amount of casing-head gasoline received or sold by the Grantee therefrom during the preceding calendar month, as the basis for computation for royalties due the State; to keep full and complete records and accounts of the operation and of the production of oil and gas and of the manufacture of casinghead gasoline derived from each and every well for which an easement is herein granted, which said records and accounts shall be available at all reasonable times to the inspection and examination by any person authorized by the State; to consent to an examination of books and records of any individual, association, or corporation which has transported for

or received from the Grantee any oil, gas or other petroleum products produced from said wells, or other wells belonging to the Grantee; to permit inspection at all reasonable times, by any person authorized by the State, of the said lands belonging to the Grantee hereinbefore described, and the said wells, improvements, machinery and fixtures used in connection therewith.

(e) To furnish, concurrently with the execution of this agreement, statements showing the quality, quantity and gravity of all oil, gas, and other petroleum products heretofore produced from said wells and manufactured from the products of said wells, and the amounts received therefor; to file, concurrently upon the execution of this agreement, with the Division of Oil and Gas of the Department of Natural Resources of the State of California, as confidential information logs of said wells, and all surveys of said wells, and any and all plats thereof, and other related information; to waive the statutory right of the Grantee to the inspection by the Director of Finance or the Chief or a duly authorized employee of either of said data and information at any time during the life of this agreement; to waive the statutory right of the Grantee to the use by the Director of Finance or the Chief or a duly authorized employee of either of any other information filed with said Division of Oil and Gas by the Grantee; to consent to the withdrawal of such logs and surveys of said wells, and any and all plats

thereof, and other related information, either in original form or by making copies thereof, from the said Division of Oil and Gas at any time during the life of this agreement, when determined desirable by the Director of Finance of the State of California, for the purpose of making public record of the same in the Division of State Lands, Department of Finance, State of California. Any and all information filed by the Grantee with the said Division of Oil and Gas shall be available at all times to the State for the purpose of forcing compliance with the terms, covenants and conditions of this agreement and rules and regulations now promulgated by the Division of State Lands and reasonable rules and regulations which may hereafter be promulgated by the Division of State Lands.

(f) To pay when due all taxes lawfully assessed and levied under the laws of the State, County, City and United States of America, upon improvements, oil gas and other petroleum products produced from the lands hereinbefore described, other than taxes on the State's royalty oil, gas and petroleum products; to accord all workmen and employees freedom of purchase and to pay wages due workmen and employees in accordance with the laws of the State of California and of the United States of America relating to employment of workmen. To comply with all laws of the State of California and all rules and regulations of any agency of the State of California having jurisdiction there-

in, and all laws of the United States of America, and all rules and regulations of any agency of the United States of America having jurisdiction therein, relating to the drilling, maintenance and operation of oil and gas wells and production of oil and gas.

(g) Not to drill into the said lands of the State of California any wells for the production of oil, gas and petroleum products, or otherwise, without the consent in writing of the Chief thereto first had and obtained; nor to redrill, lengthen or deepen without the consent in writing of the Chief first had and obtained, and then only in strict compliance with rules and regulations promulgated by the Chief, and other agency of the State having jurisdiction thereof, said wells commonly known and designated as No. 2, respectively; provided, however, if consent in writing is first had from the Chief, to redrill, lengthen or deepen any one or more of said wells commonly known and designated as No. 2 the State shall not exact any royalty or royalties in addition to those herein specified from the Grantee in consideration of the granting of such permission, and further provided, that when due to collapse of casing or other mechanical difficulty or obstruction in any of said wells, it becomes reasonably necessary to redrill any such well, the Grantee may carry on and complete the necessary work of redrilling any such well upon notice of intention, specific in detail and precise in character, of the

proposed work, being given to the State at least ten (10) days before any such work is commenced, and said work of redrilling any such well shall be done in strict conformity with the laws of the State of California and the rules and regulations promulgated thereunder by any agency of the State having jurisdiction therein without regard to whether such rules and regulations be general or specific or both; and an accurate survey of any new hole or side-tracking shall be made at intervals of not less than one hundred (100) feet, and shall immediately be filed with said Division of Oil and Gas subject to the provisions contained in subdivision "(e)" of Section "2" hereof, relating to the inspection and use by the State and withdrawal by the Director of Finance. All such operations shall be carried on in strict accordance with the detailed plan of said work as specified in such notice and be varied only with the written consent of the State first had and obtained.

(h) To exercise reasonable diligence consistent herewith in the operation of said wells while said products can be obtained in paying quantities, and not to unreasonably or unnecessarily suspend continuous operations except with the consent of the State, acting through the Chief. To carry on all operations hereunder in good workman-like manner in accordance with approved methods, having due regard for the prevention of waste of oil and unreasonable waste of gas developed through said

wells, or the entrance of water through said wells to the oil sands or oil bearing strata to the destruction or injury of the oil deposits, or future productive operations and the health and safety of workmen and employees; to plug securely, in the manner prescribed by any agency of the State having jurisdiction thereof, any well before abandoning the same so as to effectively stop the flow of water from the oil and gas bearing strata; to conduct all drilling and related productive operations subject to the inspection of authorized officials of the State; to furnish to the State detailed drawings of all oil lines in any manner attached to the said wells and to report changes or additions promptly; to gauge all oil, to measure all gas, whether dry or wet, in accordance with the rules and regulations now or which may hereafter be promulgated by the Chief, provided the State, through the Chief, shall have, at any time, the right to gauge all oil and measure all gas, and in the event of a disagreement between the State and the Grantee concerning the quality and/or quantity of the oil and/or gas so gauged and/or measured, the burden to establish the incorrectness of such gauging and/or measuring shall rest upon the Grantee, and the Grantee is hereby given the right to establish, by proper court proceeding, the correct quality and/or quantity of such oil and/or gas so gauged and/or measured; to carry out at the expense of the Grantee all reasonable orders and requirements of the State acting

through the Chief, relative to prevention of unreasonable waste and preservation of the property and the health and safety of workmen, and on failure so to do the State, through its agent or agents, shall have the right to enter on said lands of Grantee to repair or prevent such unreasonable waste at Grantee's cost; to abide and conform to the rules and regulations in force at the time this easement is granted, covering matters referred to in this paragraph, and to comply with such reasonable rules and regulations as may from time to time be issued by the State, acting through the Chief, or any other agency of the State having jurisdiction therein; provided, however, that the Grantee shall not be responsible for delay or casualties occasioned by a cause beyond the control of the Grantee.

Section 3. The State expressly reserves:

(a) The right to grant easements or crossings for wells over, under or along the courses of said wells of the Grantee, and nothing herein contained shall be construed as limiting the powers of the State of California, or of the State, to lease, convey, or otherwise transfer or encumber, during the life of this agreement, said lands of the State for any purpose whatsoever; and this agreement shall not be construed as granting to the Grantee the exclusive privilege to take oil, gas, or other petroleum products from said lands, or any portion thereof, of the State of California.

(b) Full power and authority to carry out and enforce all of the provisions of Section 15 of said

Chapter 303, Statutes of California, 1921, as amended, to the extent, if any, the same is legally applicable, to insure the sale of the production of such oil, gas and other petroleum products from said lands of the State of California to the public at a reasonable price to prevent monopoly and to safeguard the public welfare.

(c) The right to use any and all surplus gas, whether dry or wet, produced from the said wells for the purpose of repressuring the field provided that such repressuring shall not unreasonably interfere with or cause damage to the said wells of the Grantee.

Section 4. The Grantee shall assume all responsibility in connection with the maintenance and operations of said oil wells, and shall at all times hold the State free and harmless from any liability to the State, its officers, agents and employees on account of any negligent maintenance or operations on the part of the Grantee and the officers, agents and employees of the Grantee.

Section 5. In the event crossings are made or attempted to be made by others across the lands, hereinbefore described belonging to the Grantee for the purpose of entering into or upon said lands of the State of California, the Grantee shall join with the State in any course of action determined by the State for the purpose of preventing any such crossing or crossings, or if such crossings have been made, for the purpose of abatement of the same.

Section 6. This agreement does not and shall not be construed to authorize or purport to authorize any rights of way or easements to the Grantee in, through or under intervening lands for the purpose of reaching the said lands of the State of California hereinbefore described or for the purpose of maintaining and operating said oil wells in and through any land or lands other than the said lands of the State of California hereinbefore described; and further, the cost of obtaining any and all rights of way or easements necessary to effect an entrance in and to said lands of the State of California shall be at the sole cost and expense of the Grantee.

Section 7. The Grantee may use oil and/or gas produced from said wells, or gas received in exchange for such gas so produced for fuel purposes, for necessary operations of said wells on said premises, or for the drilling of new wells into said lands of the State of California, or for recirculation of any of said wells, or for repressuring the oil sand or sands from which said well may be producing, even though such gas is injected into such sand through another well, the bottom of which is in said lands of the State of California, free from any royalty charges thereon.

If and when it becomes necessary to dehydrate said oil, the Grantee may deduct the actual cost of such dehydration but not to exceed five (5) cents per barrel of net oil; such deduction shall be prior to the calculation of the royalty to the State of the said oil so dehydrated.

Section 8. The State's royalty portion of oil, gas or gasoline shall at all times be the sole property of the State, whether or not reduced to possession, and possession by the Grantee thereto at any time shall be as Trustee thereof for the State until full settlement of the royalty interests to the State shall have been made. The Grantee shall be empowered to sell and convey good title to the full amount of royalty oil, gasoline or dry gas produced and saved, if and when such sales have been approved in writing by the Chief, as herein provided.

Section 9. The Grantee may, upon the consent of the State, acting through the Chief, first had and obtained in writing, surrender and terminate this easement and agreement as a whole or as to any well covered by same upon the payment of all royalties or other obligations due and payable to the State and upon the payment of all wages due and payable to workmen and employees by the Grantee, and in no case shall such termination be effective until the Grantee shall have complied with all then existing laws relative to the abandonment of oil or gas wells.

Section 10. If the Grantee shall fail to comply with the provisions of the Act so far as applicable or make default in the performance or observance of any of the terms, covenants and stipulations hereof, or of the rules and regulations of the Division of State Lands now promulgated, and all reasonable rules and regulations which may hereafter be promulgated, and such default shall continue for the period of thirty (30) days after written notice

thereof by the State, acting through the Chief, and no steps shall have been taken within that time, in good faith, to remedy said default, then the State, acting through the Chief, may enter upon the premises of the Grantee and take possession of the same for the purpose of operating said wells of the Grantee until such time as all money defaults of the Grantee to the State have been fully satisfied, or if such default cannot be satisfied by the payment of money, then the Chief shall have the right and power to cancel the respective easement and/or to close said well or wells which are not being conducted or operated in the manner prescribed by the provisions of this easement, the rules and regulations of the Division of State Lands now promulgated, and reasonable rules and regulations of the Division of State Lands which may be hereafter promulgated; but this provision shall not be construed to prevent the exercise by the State, through the Chief, of any legal or equitable remedy which the State might otherwise effect. The waiver of or failure of the State to act upon any particular cause of forfeiture shall not prevent the cancellation and forfeiture of this easement for any other cause of forfeiture or for the same cause occurring another time.

Section 11. All notices herein provided to be given or which may be given by either party to the other shall be deemed to have been fully given when made in writing and deposited in the United States mail, registered and postage prepaid, and addressed as follows:

(To the State)
Division of State Lands
Department of Finance
State Capitol
Sacramento, California
and
(To the Grantee)
William Hazlett, Trustee,
Huntington Shore Oil Company,
918 Security Building,
Los Angeles, California

The addresses to which the notices shall or may be mailed, as aforesaid, to either party, shall or may be changed by written notice given by such party to the other as hereinabove provided; but nothing herein contained shall preclude the giving of any such notice by personal service.

Section 12. It is further covenanted and agreed that each obligation herein shall extend to and be binding upon, and every benefit hereto shall inure to, the heirs, executors, administrators, successors and assigns of the respective parties hereto. Singular shall include the plural whenever applicable and the neuter gender shall include the feminine and masculine, and vice versa, whenever used in this agreement.

Section 13. It is hereby understood and agreed that this agreement, and, all the benefits derived therefrom to the parties herein, are for the sole and exclusive benefit of the parties hereto.

Section 14. It is hereby agreed that the amount of the royalty due and payable by the Grantee to the State for all oil and gas and other petroleum products produced by the Grantee from said wells hereinbefore mentioned, up to the date of this agreement, is the sum of One Thousand Ninety Six and 28/100 (1096.28) Dollars, which the State agrees to accept and the Grantee agrees to pay in 48 equal monthly installments, commencing on the 1st day of March, 1934, and the Grantee further agrees to pay to the State interest at the rate of six (6) per centum per annum on the unpaid balance of said principal sum as the same exists from time to time, which said interest shall be due and payable annually commencing one (1) year from the date of this agreement, and annually thereafter until said principal sum is fully paid.

Section 15. It is hereby agreed between the parties hereto that this agreement may be terminated, and any of the provisions hereof may be modified and/or amended, upon the mutual consent of the parties hereto.

Section 16. This agreement, or any easement hereby granted, shall not be assigned, either in part or in whole, voluntarily or involuntarily, without the consent in writing of the Chief first had and obtained.

Section 17. The easement granted by this instrument is more specifically described as follows, to-wit:

An easement in and to, under and through, said lands of the State embracing and consisting of

separate and distinct cylindrical areas, each 24 inches in diameter and extending throughout the full length, course and distance of said respective wells herein before mentioned, in so far as the same traverse ore are in, upon or under said lands of the State, the center line of each of said respective cylindrical areas being the center line of each of said respective wells as disclosed by the surveys or plats thereof filed with the said Division of Oil and Gas of the said Department of Natural Resources and/or as verified or altered by subsequent survey, if any, and in addition thereto, similar cylindrical areas following the respective courses and directions of the center lines of such other wells as may hereafter be drilled by Grantee into and through the lands of the State with the written consent of the State or Chief, as hereinbefore provided, together with the right, under and in compliance with the terms of this instrument, to enter in and upon and to use said easement, or cylindrical areas for the purpose of conducting therein or thereon the operations authorized by the terms of this agreement.

In the event any agreement or agreements are hereafter entered into between the State acting through the Director of Finance and/or the Chief of the Division of State Lands, and persons, firms, or corporations other than the Grantee herein, pursuant to the authority under which this agreement is made, which said agreement or agreements shall relate to the taking of oil, gas, and petroleum prod-

ucts from said lands of the State of California through wells drilled upon lands of Seventeenth Street Addition to the City of Huntington Beach, California, the Grantee shall have the option to adopt the form of any such agreement in toto, in lieu of this agreement, effective from date of such adoption which shall not be later than ninety (90) days after Grantee has knowledge of any such new agreement or agreements.

Section 18. Should the State elect to take its royalty oil or dry gas in kind, notice of thirty (30) days shall be given to the Grantee of the State's intention so to do; on such election, the State shall continue to take its said royalty oil and/or dry gas (as the case may be) in kind for a period of six (6) months from the time it commenced to take such royalty oil and/or dry gas (as the case may be) in kind, and thereafter for like periods of six (6) months unless the State shall, at least thirty (30) days prior to the end of any such six (6) months' period, notify the Grantee in writing of the State's election to cease taking its royalty oil and/or dry gas (as the case may be) in kind, and to take the same in value.

Anything to the contrary herein notwithstanding, the Grantee, if operating a refinery, and if the State is not then taking the same in kind, may use such oil or gas, and account to the State for the State's royalty in accordance with the provisions of this agreement.

In witness whereof, the parties hereto have executed or caused to be executed this agreement, the day and year first above written.

STATE OF CALIFORNIA
By ROLLAND A. VANDEGRIFT
Rolland A. Vandegrift
Director of Finance
By W. S. KINGSBURY
Chief of the Division of State Lands
Department of Finance

Form approved March 12, 1934.
U. S. WEBB
Attorney General of California

[Seal] HUNTINGTON SHORE OIL COMPANY
By W. M. CRAWFORD
President
By J. D. STERLING
Secretary

Executed Oct. 19, 1904.
WILLIAM HAZLETT
William Hazlett,
As Trustee for Huntington Shore Oil Company

Executed June 24, 35.
CHARLES R. DETRICK
Mgr.
Huntington Shore Oil Company

HUNTINGTON SHORE OIL COMPANY
HOLDERS OF LAND OWNERS PERCENTS

Helen N. Adams	1/2 of 1%	By J. D. Sterling	(Attorney-in-Fact)
Felix Aubuchon & Mrs. Felix Aubuchon	1/8 of 1%	By J. D. Sterling	" "
Rosa L. Boyd	1/8 of 1%	By J. D. Sterling	" "
Albert A. Bernstein	1/8 of 1%	By J. D. Sterling	" "
Edwin Bramson	1/2 of 1%	By J. D. Sterling	" "
Ada O. Bisbee	3/8 of 1%	By J. D. Sterling	" "
Nellie E. Cunningham	1/3 of 1%	By J. D. Sterling	" "
Vincent C. & Mary J. Croal	1/4 of 1%	By J. D. Sterling	" "
H. L. Crane and Mabel C. Crane	1%	By J. D. Sterling	" "
Martha Jean Crane	1/8 of 1%	By J. D. Sterling	" "
Mrs. L. Orville Coate	1/4 of 1%	By J. D. Sterling	" "
Wilber T. Chaffee	1%	By J. D. Sterling	" "
Jasper M. & Amy Chamberlain	1/4 of 1%	By J. D. Sterling	" "
Jennie B. Durkee	1%	By J. D. Sterling	" "
Effie L. Douglas	1/3 of 1%	By J. D. Sterling	" "
Elizabeth Decker	1/2 of 1%	By J. D. Sterling	" "
Edna J. Decker	1/3 of 1%	By J. D. Sterling	" "
Helen and Mary Errebo	1%	By J. D. Sterling	" "
Fannie E. Finley	1/8 of 1%	By J. D. Sterling	" "
Caroline E. Fisk	1/4 of 1%	By J. D. Sterling	" "
Berta L. Gregory	1/3 of 1%	By J. D. Sterling	" "

Joe Goussak & Ada Goussak	1/2 of 1%	By J. D. Sterling	(Attorney-in-Fact)	
William Gosau and Edna Gosau	2%	By J. D. Sterling	"	"
H. M. Gilmore or Lula F. Gilmore	1/4 of 1%	By J. D. Sterling	"	"
Rosa L. Gilmore	1/8 of 1%	By J. D. Sterling	"	"
Anna M. Hasenyager	1/8 of 1%	By J. D. Sterling	"	"
Rosa Heller	1/4 of 1%	By J. D. Sterling	"	"
Mrs. Gussie Houssels	1/4 of 1%	By J. D. Sterling	"	"
T. H. Hawkins	1%	By J. D. Sterling	"	"
Grace M. Hawkins	1%	By J. D. Sterling	"	"
John R. Johnson & Vera Johnson	1/2 of 1%	By J. D. Sterling	"	"
Effie A. Kettrey	1/8 of 1%	By J. D. Sterling	"	"
Florence Karker	1/3 of 1%	By J. D. Sterling	"	"
John Kniss & Thelman Kniss	1/2 of 1%	By J. D. Sterling	"	"
John T. Kearns & Francis E. Kearns	1%	By J. D. Sterling	"	"
Zena Kapelman as Trustee for Esther Kapelman and Annie Kapelman	1/2 of 1%	By J. D. Sterling	"	"
Charles Kratsch and Charlotte Kratsch	1/3 of 1%	By J. D. Sterling	"	"
Carter H. Lane	3/8 of 1%	By J. D. Sterling	"	"
Fred Lovett	1/8 of 1%	By J. D. Sterling	"	"
Mary A. Leslie	1/3 of 1%	By J. D. Sterling	"	"
Florence E. Markle	1/4 of 1%	By J. D. Sterling	"	"
Sadie McConaughy	1/8 of 1%	By J. D. Sterling	"	"
Frank A. Moulton & Margaret V. Moulton	1/3 of 1%	By J. D. Sterling	"	"

Flora Moore	1/8 of 1%	By J. D. Sterling	(Attorney-in-Fact)	
Alice McClelland	1/6 of 1%	By J. D. Sterling	"	"
Nellie P. Mooers	1/8 of 1%	By J. D. Sterling	"	"
Ada M. Miner	1/4 of 1%	By J. D. Sterling	"	"
Vanie Norris	1/8 of 1%	By J. D. Sterling	"	"
Nathan Nash	1/2 of 1%	By J. D. Sterling	"	"
George I. Orenstein	1/2 of 1%	By J. D. Sterling	"	"
Sam N. Oresntein	1/2 of 1%	By J. D. Sterling	"	"
Lewis and/or Mattie and/or Nellie G. Pendleton	1/4 of 1%	By J. D. Sterling	"	"
Minnie Patrick	1/8 of 1%	By J. D. Sterling	"	"
Emma D. Richardson	1/8 of 1%	By J. D. Sterling	"	"
William H. and/or Anna Rifkind	1/2 of 1%	By J. D. Sterling	"	"
Joseph F. Reed or Agnes Reed	1/8 of 1%	By J. D. Sterling	"	"
Henry C. Roher	1/8 of 1%	By J. D. Sterling	"	"
Alice M. Sexton	1/4 of 1%	By J. D. Sterling	"	"
D. L. Sylvester or Kate B. Sylvester	1/3 of 1%	By J. D. Sterling	"	"
Elmer R. Stokesbury	1%	By J. D. Sterling	"	"
Louis and Sylvia Solomon	1/2 of 1%	By J. D. Sterling	"	"
Nat Shipper and Betty Shipper	1/4 of 1%	By J. D. Sterling	"	"
Harvey Snyder or Ruth Snyder	1/2 of 1%	By J. D. Sterling	"	"
J. W. Stokesbury	1%	By J. D. Sterling	"	"
Iona S. Sharp	1/2 of 1%	By J. D. Sterling	"	"
Katherine E. Smith	1/4 of 1%	By J. D. Sterling	"	"

M. J. and J. J. Thompson	1/3 of 1%	By J. D. Sterling	(Attorney-in-Fact)	
Ella M. Teeple	2%	By J. D. Sterling	"	"
Abe Ullman and Sara Ullman	1/2 of 1%	By J. D. Sterling	"	"
Louis Ullman and Annie Ullman	1/2 of 1%	By J. D. Sterling	"	"
Zillah Van Arsdale	1/8 of 1%	By J. D. Sterling	"	"
Sarah J. Woods	1%	By J. D. Sterling	"	"
Sara M. Wright	1%	By J. D. Sterling	"	"
Cora D. Whipple	1%	By J. D. Sterling	"	"
Bertha Woods Walker	1/4 of 1%	By J. D. Sterling	"	"
Texanna Wood	1/4 of 1%	By J. D. Sterling	"	"
Jacob Yaruss	1%	By J. D. Sterling	"	"
Joseph P. Zimmer	1/4 of 1%	By J. D. Sterling	"	"
Celestine R. Young	1/8			
	1/2 of 1%	By J. D. Sterling	"	"

[Endorsed]: Tr. Exhibit No. 2. Filed April 26, 1940. Ernest R. Utley, Referee.

[Endorsed]: Filed Mar. 28, 1941. R. S. Zimmerman, Clerk.

TRUSTEE'S EXHIBIT No. 3

State Lands Commission
Division of State Lands
Department of Finance
State of California

CERTIFICATE

I, Webb Shadle, Executive Officer of the State Lands Commission of the State of California, do hereby certify the attached to be a full, true and correct copy of a memorandum dated February 14, 1940, from Tracy L. Atherton to Webb Shadle, on file in the office of the State Lands Commission, Room 302 California State Building, Los Angeles, California; that I have compared the same with the original and that it is a correct transcript therefrom and of the whole of the said memorandum.

Witness my hand this 26th day of March, 1941.

WEBB SHADLE

State of California
Department of Finance
Division of State Lands

Date February 14, 1940

Office: Los Angeles
To: Webb Shadle—Los Angeles
From: T. L. Atherton
Subject: Proposed redrill—Easement No. 290-1

A study of the surveys as plotted and their intersection with the inclined planes shows that under our present rule it would be impossible to redrill the well under the above easement as at the following

inclined planes the well 290-1 is located within 100 feet of the well or wells as indicated.

Inclined plane	
3600 ft.	Clear
3700 "	309-2A
3800 "	309-2A and Wil. 18
3900 "	309-" " " "
4000 "	"
4100 "	Clear

TRACY L. ATHERTON (Signed)
T. L. A.

Copy
Intradivision Memorandum

[Endorsed]: Tr. Exhibit No. 3. Filed March 27, 1941. Ernest R. Utley, Referee.

[Endorsed]: Filed March 28, 1941. R. S. Zimmerman, Clerk.

TRUSTEE'S EXHIBIT No. 4

Huntington Beach Townsite Association

SUB-SURFACE CROSSING PERMIT

Permit from Huntington Beach Townsite Association, a corporation, hereinafter referred to as "Association", to Huntington Shore Oil Company, a member of said Association, hereinafter referred to as "Member".

Article I.

1. The Association has simultaneously with the acceptance by Member of this permit, entered into

an agreement with Standard Oil Company of California, and others, hereinafter referred to as "Standard Oil Agreement", a copy of which said agreement is attached to and made a part of this agreement and marked Exhibit "A".

2. Subject to the terms, conditions and limitations of this permit hereinafter set forth, and by virtue of the right and power given to Association by said Standard Oil Agreement, and for the same period as given by said Standard Oil Agreement to this Association, Association hereby gives Member a sub-surface crossing permit for Member's well in the City of Huntington Beach, California, known and designated as Huntington Shore Oil Company Well and the right to use, maintain, repair and operate said well in its existing location and course under, through and across lands of those corporations designated as "Permittors" in said Standard Oil Agreement, within the strip of land described as follows:

> In the City of Huntington Beach, California, extending from the oceanward projection of the westerly side of 13th Street to the oceanward projection of the easterly side of 23rd Street between the landward side of Ocean Avenue and the high tide line.

Article II.

This permit is given upon and subject to each and all of the terms and conditions, limitations and stipulations hereinafter set forth, and upon accept-

ance hereof Member thereby agrees to, and agrees to be bound by, all of said terms, conditions, limitations and stipulations.

1. This permit is, and at all times shall be, subject in each and every particular to the terms, conditions and stipulations of said Standard Oil Agreement, and that any revocation or cancellation or termination of the permit given Association by said Standard Oil Agreement shall automatically revoke or cancel or terminate this permit.

2. All statements, representations, descriptions, plats, surveys and data which said Standard Oil Agreement states have been made or furnished by Association to Permittors named in said Standard Oil Agreement, were made or furnished to Association by Member for the purpose of enabling Association to make or furnish them to the said Permittors, and shall be deemed to have been made direct by Member to said Permittors in order to induce said Permittors to give said permit to Association, and that all thereof are true and accurate.

A. Member, with reference to said well, shall and does hereby assume each and every responsibility, duty and obligation imposed by said Standard Oil Agreement on Association; and Member shall and does hereby relieve Association from all such responsibility, obligation and duty; and shall at all times hold and keep Association free and harmless from any and all liability, cost or expense; and should Association make any payment, or incur any expense by reason of any obligation or duty men-

tioned in this paragraph and imposed upon it by said Standard Oil Agreement, Member shall immediately on demand of Association reimburse Association therefor.

4. This permit is personal to the Member with reference to said well. It shall not be assigned in whole or in part without the written consent of the Association; furthermore, any act or circumstance which, under and by virtue of the terms of said Standard Oil Agreement, would authorize said Permittors to terminate the permit given to the Association by said Standard Oil Agreement, or to do or take any other act, shall also authorize and empower the Association to terminate this permit, or to do or take any such other act.

5. Should the Association incur any cost or expense in enforcing or effectuating this agreement Member shall repay the same to the Association upon demand.

6. Upon the termination of this permit, whether by expiration of its term or by act of said Permittors or by act of this Association or otherwise, Member agrees to abandon and plug said well in the manner provided for in Condition (d) of said Standard Oil Agreement, but if Member fails to commence the work of abandoning within ten (10) days after such termination, and thereafter fails to diligently prosecute the same to completion, Association shall have the right to enter the lands of Member, as the agent of Member, and at the

risk of Member to abandon and plug such well in such manner as the Association may deem proper, or as may be required by said Permittors, and all cost and expense of such abandonment and plugging shall be paid by Member to the Association upon demand; and in case of suit to collect the same Member agrees to pay the Association in addition a reasonable attorney's fee to be fixed and allowed by the court.

7. Any notice, information or data to be given the Association by virtue of the terms of this agreement shall be delivered in writing personally to an Officer of the Association at the office of the Association, or shall be mailed by registered mail, postage prepaid, to the Association at Huntington Beach, Orange County, California.

8. Any notice or demand to be given to Member by the Association shall be by mailing notice thereof to the Member by registered mail, postage prepaid, at the following address: Hubert F. Laugharn, 633 Subway Terminal Bldg., Los Angeles, Calif. or at such other address in the County of Orange or the County of Los Angeles, State of California, as Member may from time to time designate in writing by notice to the Association, given as herein required.

9. Subject to all the terms and conditions of this permit, it shall be binding upon the successors and assigns of the parties hereto.

In Witness Whereof, Huntington Beach Townsite Association has executed this permit in dupli-

cate on the 11th day of (initialed H.S.H.) May, 1937 (initialed H.S.H.)

[Seal] HUNTINGTON BEACH TOWN-SITE ASSOCIATION,

By EUGENE [Illegible]
President.

H. S. HANCOCK
Asst. Secretary.

Accepted:

HUBERT F. LAUGHARN
Trustee for Huntington Shore Oil Company, Bankrupt

.....

Member

HUBERT F. LAUGHARN
Trustee for Jack Dave Sterling, Bankrupt

HUBERT F. LAUGHARN
Trustee for Jack Dave Sterling, Bankrupt
(Huntington Investment Corporation)

HUBERT F. LAUGHARN
Attorney in Fact for royalty interests as per attached list

Huntington Shore Oil Company

List of names of persons having interests in the Huntington Shore Oil Company, and Huntington Shore Well #2 who have given powers of attorney

to Hubert F. Laugharn to execute the surface crossing permit, to-wit:

R. H. Garrison
H. S. Fentress
Elmer R. Stokesbary
Mrs. Jeanette Stokesbary
Wm. H. Rifkind
Mrs. Anna Rifkind
Rosa L. Boyd
George R. Finley, Executor Estate Fannie E. Finley
Fanny A. Larson
Evangeline Adams Spozio
Marion Adams
Louis Solomon
Sylvia Soloman
David W. Butler
Ralph J. Brown
Preston R. Wyrick
Anglo California National Bank of San Francisco, by A. N. Baldwin, Vice President and R. H. Holmberg, Assistant Secretary.
Henry C. Roher
Mrs. Edna L. Gosan
William Gosan
Joe Goussak
Ada Goussak
Albert G. Berenstein
Charlotte E. Berenstein
Sam N. Orenstein
Faye Orenstein

George I. Orenstein
George A. Coffey
Spencer E. Sully
Katherine E. Smith
Max Drefke
Mathilda Drefke
Fred Lovett
Virginia Rickman
Nat Shipper
Betty Shipper
Harry Oreck
Rose Oreck
Mary Errebo
Mrs. L. Orrille Coate
Mr. I. Searles, Attorney in fact for E. T. Chese
Golden Gate Oil Co., by H. R. Hamilton, President and S. F. Ballif, Jr., Secretary
John R. Kennedy
Peter Oreck
Sarah Oreck
Mrs. Lucy K. Latham
Herbert R. Kendall
Emma F. Hale
L. O'Rourke
Herbert M. Baruch
C. E. Parkman
Mrs. Kitty Parkman
George P. Wilson
C. P. Robinson
Sarah J. Woods

Florence E. Markle
Bertha Woods Walker
Mrs. Gussie Houssels
Celistine R. Young
Mary A. Leslie
Lewis Pendleton
Mattie Pendleton
Joseph P. Zimmer
Robert E. Gilmore
Ross L. Gilmore
Iona S. Sharp
Vera Johnson
Jasper N. Chamberlain
Sadie McConoughy
Harvey B. Snyder
Edna J. Decker
Elizabeth Decker
James J. Thompson
W. J. Thompson
Homer M. Gilmore
Lulu Gilmore
Nellie E. Cunningham-Beyer
Herman Sterling
Leo Pearlston
Dayton H. Boyer
Joseph Smooke
Pacific National Bank of San Francisco, Trustee under selected Income Royalties No. 2., by D. W. Holgate, Trust Officer.
Joseph F. Reed

Agnes Reed
Zena Kapelman
Harvey F. Nelson
Earl Foremaster
Frans Nelson Petroleum Company, by H. F. Nelson, President
Esther Strin
Lena Abramson
Morris Abramson
Meyer M. Brill
Cele Brill per W.M.B.
Jack Strin
Nathan Smooke
Ben Sterling
David B. Rosenthal

HUBERT F. LAUGHARN
Attorney-in-Fact for above per cent holders in accordance with powers of attorney attached hereto.

Huntington Shore Oil Company
(Jack Dave Sterling, Bankrupt)

The following are names of royalty interests not located by the undersigned Trustee:

Minnie M. Kruse
Flora Moore
Violet Olmstead
Anna Hasenyager
R. A. Calhoun

C. W. Patrick
Jennie B. Durkee
Caroline E. Fish
Carter H. Lane
Minnie Patrick
Frank A. Moulton
Commonwealth Trust Company, Trustee for Empire Investors Trustee, Series A

HUBERT F. LAUGHARN
Trustee of Jack Dave Sterling (Huntington Shore Oil Company)
Bankrupt.

Holders of royalty interests on which no final determination of validity has been made, the same held as security only.

Oil Well Supply Company
Bank of America National Trust & Savings Association

HUBERT F. LAUGHARN
Trustee of Jack Dave Sterling (Huntington Shore Oil Company)
Bankrupt.

Agreement between Standard Oil Company of California, a corporation, Huntington Beach Company, a corporation, Pacific Electric Railway Company, a corporation, and Pacific

Electric Land Company, a corporation, first parties, hereinafter collectively referred to as "Permittors", and Huntington Beach Townsite Association, a corporation, hereinafter referred to as "Association", second party:

The Association has entered into an agreement, hereinafter referred to as "Association Agreement, dated as of April 30, 1934, with Huntington Shore Oil Company, hereinafter referred to as "Member", relative to the well of said Member designated as follows, to-wit: Huntington Shore Oil Company Well, hereinafter referred to as "Well".

Subject to the terms, conditions and limitations hereinafter set forth, Permittors hereby give the Association, and the Association may in turn give said Member, a sub-surface crossing permit for, and the right to use, maintain, repair and operate, said Well in its existing location and course under, through and across lands of the Permittors within the strip of land described as follows:

In the City of Huntington Beach, California, extending from the oceanward projection of the westerly side of 13th Street to the oceanward projection of the easterly side of 23rd Street between the landward side of Ocean Avenue and the high tide line.

Any such permit given by the Association to said Member shall be subject in each and every particular to the terms, conditions and stipulations of this

permit; and any revocation or cancelling of this permit shall automatically revoke or cancel any such permit given by the Association to said Member.

The Association has furnished the Permittors with a statement specifying the above described Well and giving a particular description of the land upon which the derrick of said Well is located; the Association has also furnished Permittors with plats and surveys of said Well showing the existing location and course of said Well, and a statement of the casing maintained in said Well giving the diameter and length of each string of casing and the depth at which each string is landed. The Association hereby represents that to the best of its knowledge and belief said statements and plats are accurate.

This permit is given at the request of the Association and in reliance upon and in consideration of representations by the Association and is also given at the request of the Director of Finance and Chief of the Division of State Lands of the Department of Finance of the State of California, in order that said Member may obtain and produce, through his or its Well, oil, gas and other hydrocarbon substances from the tide and submerged lands of the Pacific Ocean under compromise agreement between the State of California, through its said Director of Finance and Chief of the Division of State Lands, and the said Member, dated March 1st, 1934,

and this permit, subject to the limitations, representations and conditions hereinafter set forth, is given for the duration of and shall run concurrently with said compromise agreement, and each and every extension or renewal thereof. COPY OF SAID COMPROMISE AGREEMENT IS HERETO ATTACHED.

This permit is given in consideration also of the following representations made to the Permittors by the Association with reference to the said Well, all of which representations the Association is informed and believes are true and accurate, and all of which representations shall be deemed to have been made direct by the Member owning or operating said Well to the Permittors upon the acceptance by such Member of the permit from the Association above referred to:

1. That said Member is the owner or entitled to the possession of the land upon which the derrick of his or its said Well is located AND IS IN ALL RESPECTS ENTITLED AND QUALIFIED TO MAKE AND ENTER INTO THE STIPULATION HEREOF WITH REFERENCE THERETO AND TO SAID WELL; said land is hereinafter sometimes referred to as the "land of the Member".

2. That said Well originates on the land of the Member owning or operating said Well and is slanted or deflected therefrom through lands of Permittors within the strip hereinabove described

into the land under the Pacific Ocean, that said Well does not terminate otherwise than or take a course substantially different from that shown on the plats and surveys of said Well furnished by the Association to Permittors hereunder, and that no portion of the perforated pipe in said Well lies within the confines of any lands of Permittors.

3. That said Well is completed and producing, or is capable of being produced FROM LAND UNDER THE PACIFIC OCEAN, and that in the drilling and construction of said Well the Member owning or operating it has used and installed therein materials and equipment of good quality and condition.

4. That the casing maintained in said Well is of the diameters and lengths and is landed at the depths specified in the statement furnished by the Association to the Permittors; that all of said casing was at the time of installation new or in good condition and was installed in a proper and workmanlike manner; that all water sands have been effectively and in a proper manner plugged off; that any and all information and survey data now or hereafter in possession of, or available to, said Member relative to the history, location, course, mechanical condition, equipment, pressures, water shut-offs, oil production, perforations and condition of said Well, and any such information now or hereafter in possession of or available to the Association is now and will be available to Permittors.

5. That said Well throughout its course is in a safe condition and does not in any wise interfere with or endanger existing wells or any other property of the Permittors. That the existence, underground location and course of said Well have been ascertained by directional survey thereof and the results of such survey have been furnished to Permittors.

This permit is given subject to the following terms and conditions, all of which are binding on the Association and such Member with reference to the said Well upon the acceptance by the Member owning or operating said Well of the permit from the Association above referred to:

(a) Said Well shall at all times be maintained and operated in a good and workmanlike manner and so as to prevent and avoid danger of injury or damage therefrom to the property of Permittors. Permittors shall at all reasonable times have right of access to said Well and to all records and survey data pertaining thereto as to the history, location, course, mechanical condition, equipment, pressures, water shut-offs, oil production, perforations and condition of said Well.

The Association and said Member, with reference to the said Well, shall at all times promptly and effectively take precautionary or other measures to protect the Permittors and their property from injury or damage from said Well, and will promptly comply with the request of the Permittors to take such precautionary or other measures.

No work shall be done on said Well without written notice by the Association, or the Member owning or operating such Well, and the proper officer of the State of California to Permittors, showing the nature of the work proposed to be done and written permission from Permittors to proceed therewith; such permission will be given only when so requested by the State of California and the proposed work, in the opinion of Permittors, will not injure, damage or jeopardize the property of Permittors or any existing or contemplated well of Permittors; provided that no notice to, or consent by, the Permittors shall be required in event said Member desires to, or does, bail or clean out said Well, change the position of, pull, or fish for, tubing in said Well, clean out or wash perforations of same, fish for foreign objects in same, place packer on said tubing, replace or change position of tubing-catcher in same, or place, pull or replace pumps, or fish for or replace sucker rods in said Well.

If for any reasons operations of said Well are voluntarily suspended for six (6) months, Permittors shall have the right to terminate this permit.

(b) Permittors shall not be liable for any injury, damage or loss to the Association or said Member, or to any well drilled, operated or maintained by any Member, or to any property of the Association or said Member, resulting from activities of Permittors on or in any property of Per-

mittors in the Huntington Beach Oil Field through which said Well may pass.

(c) The Association and said Member, with reference to the said Well owned or operated by such Member, (1) shall protect and hold Permittors harmless from any and all claims for loss, damage or injury to others, including costs and reasonable attorneys' fees in the event suit is brought, and shall pay any loss, damage or expense which Permittors may suffer or incur, arising out of or in any way connected with the existence and/or operation of said Well and from any operation or activity of the Association and such Member on, in or in connection with said Well and from or on account of any contact, collision or other interference of said Well with any other well, whether of Permittors, of any other Member or of others, on, in or which crosses the property of Permittors; (2) shall assume all risk and shall be accountable for anything occurring on account of or due to the existence or operation of said Well and shall protect, indemnify and hold the Permittors harmless THEREFROM AND against any and all injury, damage or loss arising out of or due to the enjoyment of this permit; (3) shall protect, indemnify and hold harmless Permittors and the land of Permittors from any and all mechanics' and/or other liens and any and all cost or expense incurred on account thereof arising out of, ASSERTED, or in any manner due to anything done or caused to be done on or in connection with said Well.

(d) If, as and when said Well is abandoned, the Association and the Member owning or operating such Well shall promptly abandon the same in accordance with the regulations of the State of California Department of Natural Resources, Division of Oil and Gas, and, in addition thereto, shall promptly and effectively plug with cement, in a good and workmanlike manner, such portion or portions of the same and take such precautionary and protective measures with reference thereto, as may, in the determination of Permittors, be necessary or proper to prevent any injury or damage to or interference with the property or wells of Permittors.

(e) The Association and said Member shall, on request of Permittors, submit all data, surveys and information respecting said Well relating to its history, location, course, mechanical condition, equipment, pressures, water shut-offs, oil production, perforations and condition, and all data and information as to any and all negotiations and/or arrangements for surveying said Well and all surveys thereof, whether "single shot" or otherwise, and whenever such surveys have been made, whether before or after the date hereof. If any data, survey or information furnished Permittors hereunder is incorrect or for any reason, in the judgment of Permittors, insufficient, the Association and the Member owning or operating such Well, will, on being notified of that fact, promptly furnish the required information, including survey thereof, if

required by Permittors, and if the Association or such Member fails to furnish the data, survey and information so required, Permittors, or the nominee of Permittors, shall have the right, as the agent of such Member and at such Member's and/or the Association's risk and expense, to enter upon such Member's lands and make such examination as may be necessary to obtain the desired information, including survey of said Well. In the event Permittors, or the nominee of Permittors, should be denied access to said Well for the purpose of making such examination or survey, Permittors shall have the right to terminate this permit.

(f) In the event it should be determined at any time hereafter by Permittors that any portion of the perforated pipe in said Well lies within the confines of any lands of Permittors, Permittors shall have, in addition to any other remedy, whether at law or in equity, against the owner or operator of such Well, the right to terminate this permit.

(g) Should said Well be so close to any well PROPOSED TO BE drilled by Permittors on any land owned or leased by Permittors as, in the JUDGMENT of Permittors, to injure, damage, interfere or conflict with OR JEOPARDIZE the same, Permittors shall have the right at any time after commencement of drilling operations of such well to terminate this permit whereupon the Member and/or the Association shall PROMPTLY abandon and plug said Well, as provided in condition (d) hereof.

(h) Said Member, with reference to said Well, shall comply with all laws of the State of California and all rules and regulations of any agency of the State of California having jurisdiction therein, and all laws of the United States of America, and all rules and regulations of any agency of the United States of America having jurisdiction therein, relating to the drilling, maintenance and operation of oil and gas wells and production of oil and gas.

Said Member, with reference to said Well, shall comply with any reasonable conservation or curtailment program or programs which may at any time and from time to time affect the production of oil and/or gas from the said Well, and which program or programs are mutually agreed upon by a majority of the operators in the field in which such Wells are situated.

(i) This permit is personal to the Association and to such Member with reference to the said Well, and shall not be assigned, in whole or in part, without the written consent of Permittors. In the event this permit is assigned as to said Well, whether voluntarily or by operation of law, or in the event such Well is operated or controlled by one who is not a Member of the Association, Permittors shall have the right to terminate this permit as to such Well; provided, however, that in the event the land on which the derrick of said Well is located, together with the Well and its equipment is repossessed by the lessor of said Member, such repossession shall not be construed as an assignment,

and in such event Permittors shall not terminate this permit, provided such lessor becomes, immediately after such repossession, a member of the Association AND MAKES GOOD ANY FAILURE OF THE PERMITTEE TO FULLY PERFORM ANY UNFULFILLED PROVISION HEREOF. Subject to all the terms and conditions hereof, this permit shall be binding upon the successors and assigns of the parties hereto.

(j) Any and all cost or expense incurred by Permittors in enforcing or effectuating this agreement will be repaid to Permittors on demand by the Association and the Member owning or operating said Well.

(k) Should any of the foregoing representations fail with reference to said well, or should the Association or said Member be in default in the strict and faithful observance of any of the foregoing conditions with reference to said Well, or should such Member cease to be a member of the Association, or should such Member fail faithfully to comply with his or its obligations under said Association Agreement, or fail to comply with any of the terms or conditions of any permit, which, by virtue of this agreement, the Association may give to such member, Permittors shall have the right immediately to terminate this permit as to the said well.

(l) Upon the termination of this permit, whether by expiration of its term, or otherwise, the Association and said Member, with reference to the

said Well, shall abandon and plug, in the manner provided for in condition (d) hereof, the said Well, but if the Association or such Member should fail to commence the work of abandoning within ten (10) days after such termination, and thereafter fail to diligently prosecute the same to completion, Permittors, or the nominee of Permittors, shall have the right to enter the lands of such Member as the agent of such Member and to abandon and plug said Well in such manner as Permittors shall deem proper for the protection of the property or wells of Permittors, at the risk of the Association and such Member, and all cost and expense of such abandonment and plugging, together with interest thereon at the rate of seven per cent (7%) per annum, shall be paid by the Association for such Member or by such Member, upon demand; and in case of suit to enforce or collect the same, the Association, for such Member, and such Member agree to pay Permittors in addition a reasonable attorney's fee to be fixed and allowed by the court.

The Association severally agrees with the Permittors:

A. Not to give any permit hereunder except to said Member. Nothwithstanding any provision in the permit from the Association to said Member, the obligations of the Association and said Member hereunder shall remain joint and several;

B. To notify the Permittors of the breach by said Member of his or its obligations under the Association Agreement.

C. To immediately create and maintain with a depositary approved by Permittors an Indemnity Fund of not less than $100,000 for the discharge of the obligations of the Association and its Members to the Permittors hereunder, and under any similar permit, and said fund shall not be drawn upon for any other purpose. Should any portion of said Fund of $100,000 be used for such purpose, the Association will, whenever and as often as said Fund is so used, by assessment among its Members, in the manner now provided in the existing agreement between the Association and its members dated as of April 30, 1934, promptly raise said Fund to the sum of $100,000. The Association shall not draw on said fund without the written approval of Permittors to the depositary, and the Association will maintain with such depositary notice and direction to that effect, acknowledgment of which shall be sent to Permittors by Depositary.

In the event the Association should be dissolved or in the event the Association should not strictly and faithfully comply with each and all the provisions hereof, the Permittors shall have the right immediately to terminate this permit, whereupon said Well shall be abandoned subject to and in accordance with the provisions of this agreement.

The word "Permittors" whenever used in this permit shall be deemed to include and refer to the first parties herein, or any of them.

Permittors hereby designate Standard Oil Company of California, whose address is 225 Bush

Street, San Francisco, California, as their representative in all matters relating to this agreement.

Any notice, information or data to be given Permittors hereunder shall be valid if mailed by registered mail, postage prepaid, to Standard Oil Company of California at the above address; any notice or other communication to be given the Association or said Member shall be valid if mailed by registered mail, postage prepaid, to the Association at Huntington Beach, California.

If there is any conflict between the Association Agreement and this agreement with respect to the obligations of the Association and said Member hereunder, the provisions of this agreement shall prevail.

In witness whereof, the parties hereto have executed these presents as of the 5th day of July, 1935.

STANDARD OIL COMPANY
OF CALIFORNIA
[Seal] By B. W. LETCHER
Asst. Sec'y
HUNTINGTON BEACH
COMPANY
[Seal] By G. M. FOSTER
Ass't Secty
PACIFIC ELECTRIC RAILWAY COMPANY
[Seal] By D. W. PONTIUS
Pres.

PACIFIC ELECTRIC LAND
COMPANY
[Seal] By D. W. PONTIUS
Pres.
Permittors.
HUNTINGTON BEACH
TOWNSITE ASSOCIATION
[Seal] By EUGENE MELTON
Pres.
H. S. HANCOCK
Asst Secy.
Association.

Dated May 11, 1937.

[Endorsed]: Tr. Exhibit No. 4. Filed April 26, 1940. Ernest R. Utley, Referee.

[Endorsed]: Filed March 28, 1941. R. S. Zimmerman, Clerk.

Mr. Dechter: That is all for the petitioner, for the Trustee.

Mr. Borden: I think I made the statement in the first instance that our cross examination was not to be construed as any waiver of our objection to the jurisdiction.

The Referee: Oh yes.

Mr. Borden: I don't think there is any question about that. We have no evidence to offer at the present time. I might have if there is any question in your Honor's mind whether or not the Court,

in a summary proceeding of this kind against a total stranger, and under these circumstances, has a right to take any action or to restrain us from proceeding. I should like to have a continuance in order to put on some testimony without conceding the jurisdiction of the Court. I think the Court is entitled to have the benefit, no matter what order it makes with respect to directing the Trustee to commence plenary action or any other remedy available to him, of hearing testimony on both sides.

Mr. Dechter: We have no objection to giving Mr. Borden [188] a reasonable length of time.

The Referee: From what I know about this case here is the way I feel now: I don't think the bankruptcy court has any jurisdiction to tell a stranger where or how he should drill his well so long as that stranger does not interfere or trespass upon the rights of the bankrupt. Up to that point this Court has not anything to say. If there is a danger of trespassing or damaging the bankrupt's property, I think then the Court would have jurisdiction, that is, covering that particular phase of it. That is my offhand impression.

Mr. Borden: Well, I think there is no doubt if we were actually trespassing upon the property of the bankrupt, there is no doubt in my mind but what the Court would have ample opportunity to restrain us, but here we are drilling in separate lots where there is no interference at all. We are doing the same thing they have done since the matter has been in bankruptcy, your Honor. They

have drilled within one hundred feet of us, according to the testimony before the Court, but now they seek to enjoin us from proceeding to do the very same thing, to re-drill and place our well on production.

The Referee: I can say right now this Court will not attempt to prevent you from re-drilling, but there is a certain course which this Court may prevent you from taking.

Mr. Pallette: I think we can stipulate to an order, if [189] you want to make one, restraining us from coming within a certain distance.

Mr. Dechter: That is agreeable.

The Referee: What would be a reasonable distance, the regulation of the Department?

Mr. Dechter: I am willing to make it within the radius of one hundred feet, or the diameter of two hundred feet. In other words, if counsel will agree—

The Referee: Why not follow the regulation——

Mr. Dechter: That is agreeable.

The Referee: ——as Exhibit 1 provides?

Mr. Dechter: I might also call the Court's attention to the Huntington Townsite agreement which is binding on the Bolsa Chica Corporation, which contains this provision:

> "Said member, with reference to said well, shall comply with all of the laws of the State of California and all rules and regulations of any agency of the State of California having jurisdiction thereof."

Now, other members of this association have agreed to comply with those rules and this agency has jurisdiction.

Mr. Borden: That is not before this Court. It is a matter of whether or not we were interfering with the bankrupt's property.

Mr. Rifkind: I understand it is agreeable that an injunction be granted embodying the regulations——

Mr. Pallette: No. [190]

Mr. Rifkind: What is that?

Mr. Pallette: No.

Mr. Rifkind: What do you suggest?

Mr. Pallette: I suggested we would be willing to stipulate that an injunction be granted restraining us from coming within a reasonable distance of the well.

Mr. Dechter: All right.

Mr. Pallette: I think we will have to consult with our engineers as to what they deem to be a reasonable distance.

Mr. Dechter: If you make it one hundred feet it will end the matter.

The Referee: Is it one hundred or two hundred?

Mr. Dechter: Within a radius of one hundred feet or a diameter of two hundred feet.

Mr. Borden: No one ever contended we would get any closer than that.

The Referee: Suppose, gentlemen, I continue this matter and then you can see if you can get together on an order?

Mr. Pallette: I wouldn't be surprised but what we could stipulate on one hundred feet, but I don't think I am justified in doing so without consulting our engineers.

Mr. Borden: I think that is a good idea. Let the record show, if your Honor please, that by suggesting that we are willing to submit to the jurisdiction of the Court, that we do not do so until we actually do so.

The Referee: Yes, I understand that. Suppose I continue [191] this matter for a week or ten days?

Mr. Pallette: Could it be continued for a shorter time than that. We have a hearing set before the State Lands Commission some time during the middle of next week at which time we hope to get the consent of the State to proceed.

The Referee: You are not going to proceed until you do that?

Mr. Pallette: We are closed down. We have been closed down for about a week, and we have no intention of proceeding now. We hope to work out an agreement with the Chairman of the State Lands Commission some time during the week. I suggest a continuance be granted until Tuesday or Wednesday.

The Referee: Of this next week?

Mr. Pallette: Yes.

Mr. Dechter: Of the coming week, or the week following?

Mr. Pallette: Next Tuesday or next Wednesday.

Mr. Borden: I don't think it would take any time at all.

Mr. Dechter: I suggest we make it Wednesday, your Honor.

The Referee: Well, due to the condition of my calendar I will continue it until May 1st, in the afternoon, 2:00 P. M.

Mr. Rifkin: Do I understand that until that time there will be no resumption of drilling?

Mr. Pallette: That is correct, we will consent to not re-drill before next Wednesday, that is, to make any holes.

The Referee: Very well.

(Whereupon an adjournment was taken to the hour of 2:00 P. M., May 1st, 1940.) [192]

Los Angeles, California.
Wednesday, May 1, 1940.
2:00 o'Clock, P. M. Session.

* * * * * * * *

The Referee: Have you accomplished anything in the matter of Jack Dave Sterling?

Mr. Rifkin: Yes, your Honor. We have reached a stipulation that an injunction may be issued by the Court against the Bolsa Chica Oil Corporation. We have already given the specific language to the reporter and I would like him at this time to read it to the Court.

The Referee: Is the stipulation generally agreed to between counsel?

Mr. Borden: Yes.

The Referee: You may state generally what it is.

Mr. Borden: We have stipulated as to the order. We do not concede jurisdiction of the Court. We are going to agree that we will not review the order of Court and will be bound by the order. However, I make that statement because we do not want to generally concede jurisdiction.

The Referee: You may review any order this Court makes I would welcome a review—but if I were going to be reviewed on a question of jurisdiction I would want to give serious consideration to the question.

Mr. Borden: I will say you will not be required to do so; but we do not want to submit to any proceedings in a [193] court where we are strangers.

Mr. Rifkind: I would like to have the reporter read aloud our stipulation.

The Referee: Very well.

Mr. Borden: I agree with you, but I wanted our position made perfectly clear.

(Whereupon the stipulation referred to was read by the reporter, as follows:)

"Bolsa Chica Oil Corporation, its superintendent, agents and employees, shall be restrained and enjoined from drilling, re-drilling or sidetracking its Petroleum Well, also known as Fee No. 1 Well at Huntington Beach, California, so that it comes closer than 200 feet from the Huntington Shore Well measured on a horizontal plane at any point below the depth of 3800 feet below sea level as the course of the Huntington Shore Well is shown on the plat or chart marked Trustee's Exhibit 5.

"In determining whether such drilled, re-drilled or sidetracked portion of Petroleum Well, also known as Fee No. 1 Well approaches within 200 feet of the Huntington Shore Well, measured as above set forth, the course of the Huntington Shore Well in said plat shall be as dilineated on said plat and shall be conclusive as to the parties; and the distance therefrom shall be conclusively determined by plotting the course of the drilled, re-drilled or sidetracked portion of said [194] Fee No. 1 Well on said plat, based upon single shot surveys taken during the course of the drilling, re-drilling or sidetracking of the Petroleum Well, also known as Fee No. 1 Well, at approximately every 100 feet, which single shot surveys shall be made available to the Trustee in Bankruptcy or his representatives as the same are from time to time taken and made;

"That the circulating fluid in drilling, re-drilling, or sidetracking of said Petroleum Well, also known as Fee No. 1 Well, shall be virgin crude oil maintained at a grade and gravity consistent with good oil practice in said field, and that no mud or other foreign substances of any kind shall be used in lieu or such circulating fluid, provided that a substitute circulating fluid may be used as may be mutually agreed to in writing between the petroleum engineers for the respective parties thereto."

Mr. Rifkind: Now, I think there should be no cementing in the well unless agreed to between the engineers of the parties. I understand you do not contemplate any cementing and there shall be none unless that becomes a matter of discussion?

Mr. Templeton: Or unless required by law or some legally constituted authority.

Mr. Rifkind: If you engineers can agree that it is good practice, all right. [195]

Mr. Anderson: On the other hand, suppose they can't agree?

Mr. Rifkind: We will have to worry about that later; but your superintendent here now says you do not contemplate using any cement.

Mr. Anderson: But you never know what will develop.

Mr. Templeton: Should we develop a hole in the casing above our present cement shut-off it may become necessary to place a cement job in that portion of the hole, which should not in any way jeopardize the Huntington Shore Well.

Mr. Rifkind: Well, that would develop a new consideration. Right now it is not present, and when it develops it should be made a subject of inquiry.

The Referee: Why not put it in this form, if you are going to put it in at all:

> That application, if it could not be agreed upon, could be made to the Court in the way of a petition.

Mr. King: I believe the Division of Oil and Gas could take care of that.

Mr. Rifkind: If the petroleum engineers for the parties cannot agree to the use of concrete, in the event both engineers deem it necessary, the matter may be submitted to the Court, if necessary.

Mr. Pallette: What about the Division of Oil and Gas clamping down on us?

Mr. Rifkind: If they clamp down on you then there is no [196] necessity for a hearing, but on the other hand we may want to inquire into it.

Mr. Anderson: I think Mr. King will advise you there will be no need for cement in the productive interval. We do not contemplate going through the productive zone. There is no water below that horizon.

Mr. Rifkind: Is there any reason why you could not submit that to our petroleum engineer, and he may not raise the question; but on the other hand, if he does raise the question, you will have to get the permission of the Division of Oil and Gas.

Mr. Pallette: Make that in the alternative.

Mr. Rifkind: Before you do any cementing that you submit it to our petroleum engineer for consideration, and if there is any question, that we come back here and submit the proposition to the Court.

Mr. Pallette: Or to the Division of Oil and Gas.

Mr. Rifkind: All right.

The Referee: Is that stipulation agreeable, gentlemen?

Mr. Borden: Yes.

Mr. Rifkind: We will prepare an order.

The Referee: Very well, prepare a formal order.

Mr. Rifkind: It will be approved as to form and contents by both sides.

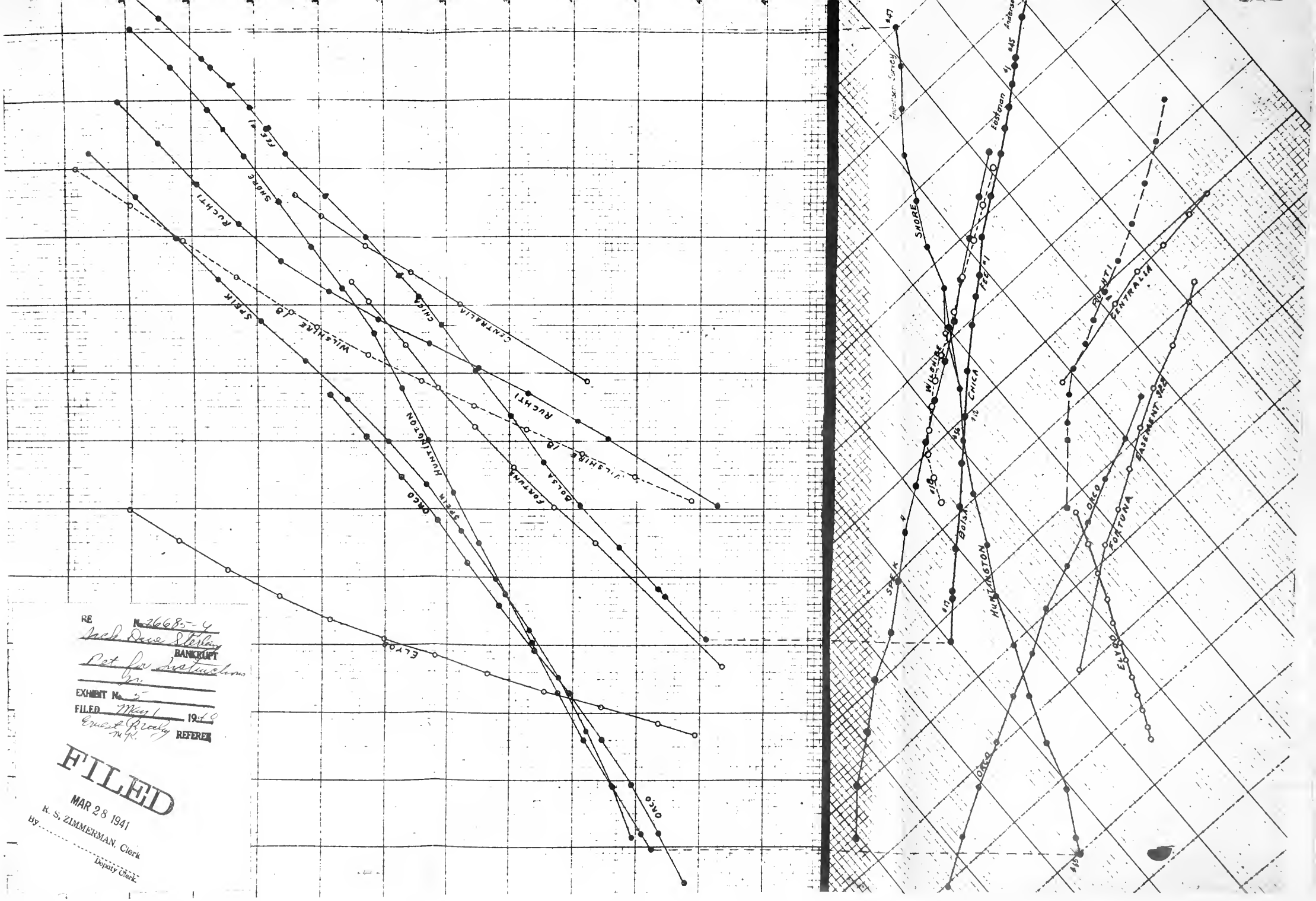
Now, I want to introduce as Trustee's exhibit next in order this plat showing among other things the course of the [197] Huntington Shore Well and the course of the old Bolsa Chica Well.

Mr. Pallette: The present course.

Mr. Rifkind: The present course of the Bolsa Chica Well, known as Petroleum Well, and also known as Fee No. 1 Well.

The Referee: The plat will be marked Trustee's Exhibit No. 5.

(The document referred to is marked Trustee's Exhibit No. 5, in evidence.)



RE No. 2668-4
Jack Dave Sterling
BANKRUPT
Ret for instructions
by
EXHIBIT No. 5
FILED May 1 1941
Ernest Brady
REFEREE

FILED
MAR 28 1941
R. S. ZIMMERMAN, Clerk
By ..... Deputy Clerk

[Endorsed]: Filed Sept. 30, 1940. Ernest R. Utley, Referee.

[Endorsed]: Filed Dec. 31, 1940. R. S. Zimmerman, Clerk. [198]

[Title of District Court and Cause.]

REPORTER'S TRANSCRIPT OF PROCEEDINGS IN RE: TRUSTEE VS. BOLSA CHICA OIL CORPORATION.

Los Angeles, California.

Thursday, September 26, 1940; Monday, September 30, 1940; Tuesday, October 1, 1940.

Appearances:

Elizabeth R. Hensel and William H. Cree, Esq., appearing specially for M. M. McCallen Corporation, McVicar and Rood, H. H. McVicar, C. M. Rood and W. H. Cree.

Overton, Lyman and Plumb, by Eugene Overton, Esq. and Warren S. Pallette, Esq., for Bolsa Chica Oil Corporation.

Joseph J. Rifkind, Esq. and Raphael Dechter, Esq., for Hubert F. Laugharn, Esq., Trustee.

W. H. Abrams, Esq., for Division of Oil and Gas. [199]

Los Angeles, California.
Thursday, September 26, 1940.
10:00 O'clock, A. M. Session.

The Referee: Jack Dave Sterling.

Mr. Rifkind: Ready.

The Referee: You may proceed in this matter.

Mr. Cree: My name is William H. Cree, Attorney at Law, 1216 Security Building, Long Beach. I am appearing here specially for M. M. McCallen Corporation, McVicar and Rood, H. H. McVicar, C. M. Rood, and myself, to object to the jurisdiction of the Court to hear and dispose of this matter, and at this time I was asked to associate Mrs. Hensel, one of your local bar, as counsel for myself and the other defendants I just named.

The Referee: May we have the other representations?

Mr. Overton: Overton, Lyman and Plumb are appearing for Bolsa Chica Oil Corporation and appearing specially, represented by Mr. Pallette and Mr. Overton. I am Mr. Overton and this is Mr. Pallette. [200]

The Referee: As I recall, when this injunction was issued counsel appearing at that time for the respondents objected to the jurisdiction of the Court. I think the Court stated at that time and I think the record will so show the Court stated it doubted its jurisdiction to prevent the drilling of the well so long as it did not interfere with [208] the bankrupt's property, that it was only in connection with any interference of the bankrupt's

property that the Court might have jurisdiction of the matter. After the objection to the jurisdiction was overruled counsel who then appeared, together with Mr. Rifkind, got together and worked out the details of the restraining order.

Mr. Rifkind: That is correct.

Mr. Dechter: I might state, your Honor, counsel in open court said they would consent to an injunction being granted along the lines stated in the order.

The Referee: Yes, that is correct.

Mr. Dechter: In other words, there was a continuance had for the purpose of having Mr. Borden discuss the matter with the engineer of the Bolsa Chica Oil Corporation to work out how many feet the Bolsa Chica Well should stay away from the Huntington Shore Well. That was the only question, if we could get together on the number of feet they would consent to the order, and mud not being used. Then they got together with the engineer——

Miss Hensel: The order itself by its terms specifically reserves the right to objecting counsel, or reserves to them the right to object to the jurisdiction.

Mr. Dechter: I don't agree with counsel.

Miss Hensel: After that later in the order the Court does overrule the objection.

Mr. Dechter: In the order itself, in addition to what [209] took place in court it states they consented to the jurisdiction of this Court to make the order in question.

Miss Hensel: Yes, but I submit——

Mr. Dechter: But reserved the right to object to the general jurisdiction of the Court as to other matters.

Mr. Rifkind: To keep the matter straight I will read from page 83 of the transcript.

Miss Hansel: I would rather straighten out the matter of the order first, and not from the transcript.

Mr. Rifkind: I will read from the transcript, page 83, line 2:

> "The Referee: From what I know about this case here is the way I feel now: I don't think the bankruptcy court has any jurisdiction to tell a stranger where or how he should drill his well so long as that stranger does not interfere or trespass upon the rights of the bankrupt. Up to that point this Court has not anything to say. If there is a danger of trespassing or damaging the bankrupt's property, I think then the Court would have jurisdiction, that is, covering that particular phase of it. That is my offhand impression.
>
> Mr. Borden: Well, I think there is no doubt if we were actually trespassing upon the property of the bankrupt, there is no doubt in my mind but what the Court would have ample opportunity to restrain us, but here we are drilling in separate lots where there is no [210] interference at all. We are doing the same thing they have done since the matter has been

in bankruptcy, your Honor. They have drilled within one hundred feet of us, according to the testimony before the Court, but now they seek to enjoin us from proceeding to do the very same thing, to re-drill and place our well on production.

The Referee: I can say right now this court will not attempt to prevent you from re-drilling, but there is a certain course which this Court may prevent you from taking.

Mr. Pallette: I think we can stipulate to an order, if you want to make one, restraining us from coming within a certain distance."

Then I will skip on to page 85:

"Mr. Pallette: I suggested we would be willing to stipulate that an injunction be granted restraining us from coming within a reasonable distance of the well.

Mr. Dechter: All right.

Mr. Pallette: I think we will have to consult with our engineers as to what they deem to be a reasonable distance.

Mr. Dechter: If you make it one hundred feet it will end the matter.

The Referee: Is it one hundred or two hundred?

Mr. Dechter: Within a radius of one hundred feet [211] or a diameter of two hundred feet.

Mr. Borden: No one ever contended we would get any closer than that.

The Referee: Suppose, gentlemen, I continue this matter and then you can see if you can get together on an order?

Mr. Pallette: I wouldn't be surprised but what we could stipulate on one hundred feet, but I don't think I am justified in doing so without consulting our engineers.

Mr. Borden: I think that is a good idea. Let the record show, if your Honor please, that by suggesting that we are willing to submit to the jurisdiction of the Court, that we do not do so until we actually do so."

And then the Referee on page 86:

"The Referee: Well, due to the condition of my calendar I will continue it until May 1st, in the afternoon, 2:00 P. M.

Mr. Rifkind: Do I understand that until that time there will be no resumption of drilling?

Mr. Pallette: That is correct, we will consent to not re-drill before next Wednesday, that is, to make any hole.

The Referee: Very well."

Whereupon an adjournment was taken to the hour of 2:00 P. M. May 1st, 1940. [212]

Now, skipping to page 87 of the transcript at the session of Wednesday, May 1st, 1940 at 2:00 o'clock, P. M.:

"The Referee: Have you accomplished anything in the matter of Jack Dave Sterling?

Mr. Rifkind: Yes, your Honor. We have reached a stipulation that an injunction may be issued by the Court against the Bolsa Chica Oil Corporation. We have already given the specific language to the reporter and I would like him at this time to read it to the Court.

The Referee: Is the stipulation generally agreed to between counsel?

Mr. Borden: Yes.

The Referee: You may state generally what it is.

Mr. Borden: We have stipulated as to the order. We do not concede jurisdiction of the Court. We are going to agree that we will not review the order of Court and will be bound by the order. However, I make that statement because we do not want to generally concede jurisdiction.

The Referee: You may review any order this Court makes—I would welcome a review—but if I were going to be reviewed on a question of jurisdiction I would want to give serious consideration to the question.

Mr. Borden: I will say you will not be required to do so; but we do not want to submit to any proceedings in [213] a court where we are strangers.

Mr. Rifkind: I would like to have the reporter read aloud our stipulation.

The Referee: Very well.

Mr. Borden: I agree with you, but I wanted our position made perfectly clear.

(Whereupon the stipulation referred to was read by the reporter, as follows:)

'Bolsa Chica Oil Corporation, its superintendent, agents and employees, shall be restrained and enjoined from drilling, re-drilling or sidetracking its Petroleum Well, also known as Fee No. 1 Well at Huntington Beach, California, so that it comes closer than 200 feet from the Huntington Shore Well measured on a horizontal plane at any point below the depth of 3800 feet below sea level as the course of the Huntington Shore Well is shown on the plat or chart marked Trustee's Exhibit 5.

'In determining whether such drilled, re-drilled or sidetracked portion of Petroleum Well, also known as Fee No. 1 Well approaches within 200 feet of the Huntington Shore Well, measured as above set forth, the course of the Huntington Shore Well in said plat shall be as delineated on said plat and shall be conclusive as to the parties; and the distance therefrom shall be conclusively determined by plotting [214] the course of the drilled, re-drilled or sidetracked portion of said Fee No. 1 Well on said plat, based upon single shot surveys taken during the course of the drilling, re-drilling or sidetracking of the Petroleum Well, also known as Fee No. 1 well, at approximately every 100 feet, which single shot surveys shall be made available

to the Trustee in Bankruptcy or his representatives as the same are from time to time taken and made;

'That the circulating fluid in drilling, redrilling, or sidetracking of said Petroleum Well, also known as Fee No. 1 Well, shall be virgin crude oil maintained at a grade and gravity consistent with good oil practice in said field, and that no mud or other foreign substances of any kind shall be used in lieu of such circulating fluid, provided that a substitute circulating fluid may be used as may be mutually agreed to in writing between the petroleum engineers for the respective parties thereto.' ''

Now, that covers that point.

Now, in connection with that I would like to point out to the Court, and I think in this matter the Court will have to take judicial knowledge that an order was prepared by counsel for the Trustee, that is an injunction and that objections were interposed thereto by counsel for the Bolsa Chica Oil Corporation, and your Honor permitted a conference [215] in chambers at which Mr. Borden, attorney for the Bolsa Chica Oil Corporation, and others, were present, and I was present on behalf of the Trustee, at which time certain revisions were made in the order, that is the injunction as originally presented, and they were incorporated in the final order.

Going back to the transcript, page 91, by the way, and referring to the stipulation which I have just read, line 19, page 91:

"The Referee: Is that stipulation agreeable, gentlemen?

Mr. Borden: Yes.

Mr. Rifkind: We will prepare an order.

The Referee: Very well, prepare a formal order.

Mr. Rifkind: It will be approved as to form and contents by both sides."

Now, in conformity with that we prepared an order and the order was revised and as revised the injunction as revised and signed by your Honor bears this notation on the last page:

"Approved as to form and contents: Joseph J. Rifkind and Raphael Dechter by Joseph J. Rifkind, attorneys for Trustee in Bankruptcy. Overton, Lyman and Plumb, by Cecil A. Borden, attorneys for Bolsa Chica Oil Corporation, a corporation."

Now, in connection with that I think the Court should [216] have in mind the preamble of the injunction:

"The verified petition of Hubert F. Laugharn, as Trustee in Bankruptcy in the above entitled matter, and the order to show cause issued thereon directed to the Bolsa Chica Oil Corporation, a corporation, came on regularly for hearing before Hon. Ernest R. Utley, Ref-

eree in Bankruptcy, on April 26, 1940, at two o'clock P. M. and after being partially heard on said date, was continued for further hearing to and the hearing thereof was concluded on May 1, 1940, at two o'clock P. M. The Trustee in Bankruptcy appeared through and was represented by Joseph J. Rifkind and Raphael Dechter, his attorneys, and the Bolsa Chica Oil Corporation, a corporation, appeared through and was represented by Cecil A. Borden and Warren S. Pallette, of Overton, Lyman & Plumb, its attorneys. The Bolsa Chica Oil Corporation, upon the calling of the matter, announced that it was appearing specially for the sole purpose of objecting to the jurisdiction of the court to make any order affecting said corporation; that thereupon the court informed counsel that it would withhold ruling upon the question of jurisdiction until sufficient evidence was introduced to determine the question; that oral and documentary evidence was introduced upon the part of the Trustee in Bankruptcy and the witnesses called on behalf of the Trustee in Bankruptcy were [217] cross-examined by the attorneys for the Bolsa Chica Oil Corporation; the Bolsa Chica Oil Corporation, having at the conclusion of the introduction of oral and documentary evidence upon behalf of the Trustee in Bankruptcy, stipulated in open court to the granting of the injunction as hereinafter more particularly set forth, the Bolsa

Chica Oil Corporation stating that such stipulation was subject to the objection to the jurisdiction of the court and that such stipulation was not intended to confer general jurisdiction on the court; the court having been fully advised in the premises and the court having overruled the objection of Bolsa Chica Oil Corporation to the jurisdiction of the court,

It Is, Therefore, Ordered as Follows:"

Then I will skip portions of the injunction which I do not deem pertinent at this moment, and turning to page 2 which incorporates that stipulation made in open court and that particular portion of it, to-wit:

"That the circulating fluid used in drilling, re-drilling or sidetracking of said 'Petroleum Well', also known as 'Fee No. 1 Well', shall be virgin crude oil maintained at a grade and gravity consistent with good oil practice in said field, and that no mud or other foreign substances of any kind shall be used in lieu or as part of such circulating fluid, provided [218] that a substitute circulating fluid may be used as may be mutually agreed to in writing between the petroleum engineers for the respective parties thereto."

Mr. Pallette: I would like the record to show Mr. Overton and I are appearing for Bolsa Chica Oil Corporation, Mr. Simmons, Mr. Anderson and myself, and Mr. Cree and his associates are repre-

senting the other respondents. Mr. Overton stated we are appearing specially and I want to amplify that and state we are appearing specially to continue at this time our objection to the jurisdiction of the Court which was not waived at the former hearing.

Miss Hensel: On behalf of Mr. Cree and myself and the clients whom we represent we urge the matter of the jurisdiction of the Court most strenuously. There can be no question that our clients waived jurisdiction at the prior hearing. We are simply wanting to point out to the Court Bolsa Chica itself did not waive that objection at the prior hearing, and now under our claim of right to the property formerly owned and operated by Bolsa Chica under an adverse title we certainly are objecting to the jurisdiction and appear specially only for the purpose of determining whether the Court has jurisdiction or not.

The Referee: Any argument?

Mr. Dechter: I think it would be preferable to defer the argument until the close. We have quite a number of cases to cite to your Honor. Even in cases where the [219] injunction has not been consented to, where there might have been some attack made on the jurisdiction of the Court, that no appeal having been taken from the order even though the order was clearly erroneously made the parties are bound by the injunction and cannot violate the injunction willfully like it has in this case. If they feel the injunction is erroneous they should apply

to have it modified or vacated. It is our contention as far as McVicar and Rood are concerned, they are agents and accessories for the Bolsa Chica Oil Corporation in the attempt to circumvent this injunction; because the Bolsa Chica Oil Corporation felt it could not do it directly it did it indirectly. Even though they were agents and accessories they would be bound by it.

Miss Hensel: In the first place, counsel will have first to prove that McVicar and Rood and the other parties are accessories and agents of the Bolsa Chica Oil Corporation. In that case if they could so prove it is conceivable the Court might have jurisdiction to issue such an injunction as this against these clients, but until it is proven beyond any doubt our clients certainly cannot be subservient to such an injunction, so we will object to the introduction of any evidence on any ground except the single ground of showing the connection between our clients and the Bolsa Chica at this time.

Mr. Dechter: An injunction having been issued and being in full force and effect we have only to show the injunction [220] is being violated, and it behooves the respondents and all of them to condone their conduct and show it did not come within the purview of the language of the injunction. We do not have to connect them up. In other words, the authorities we have, not only State Court but United States Supreme Court and various Federal Court cases are conclusive that this injunction is in full force and effect not only on those named but those

aiding and abetting those named. The only way they can escape the full force and effect of it is to take a review or appeal or some other appropriate proceeding. They cannot as long as the injunction is in full force and effect ignore, violate or disobey it, and they cannot attack the jurisdiction of the Court, the merits of the matter or the propriety of the injunction in a contempt proceeding.

I think we should present evidence, your Honor, but if your Honor deems otherwise, we are prepared with proper authorities to maintain our position.

Mr. Pallette: I think we are in position to show anyway that Bolsa Chica Oil Corporation has made a bona fide sale of the well and if that can be established, as I believe it can, it won't be necessary for you to rule on the stipulation as far as Bolsa Chica Oil Corporation is concerned.

Now, I suggest a stipulation with counsel reserving our objections to the jurisdiction and making an objection to the introduction of any evidence to be determined by the [221] ruling on the question of jurisdiction, and if we are not successful in satisfying you on our position in the matter that we reserve argument on the question of jurisdiction until after the introduction of such evidence.

Mr. Dechter: We do not care to make any such stipulation. We are contending the Bolsa Chica Oil Corporation is estopped from making any such objection. As far as the Court ruling on the objection to the jurisdiction, it is well established in

bankruptcy courts that the bankruptcy court has the right to hear enough evidence to determine whether the objection to the jurisdiction is bona fide or not. In other words, you cannot make it on the mere statement of counsel and not inquire into the matter to determine whether it has or has not jurisdiction. [222]

The Referee: Well, gentlemen. The Court will overrule the objection to the jurisdiction without prejudice to the right of the parties to renew their objection at the close of the evidence. [226]

EARL ROSS,

called as a witness on behalf of the Trustee, being first duly sworn, testified as follows:

The Referee: Give your full name to the reporter. A. Earl Ross.

The Referee: Where do you reside?

A. 121 Kansas Street, Arcadia.

Direct Examination

By Mr. Rifkind:

Q. What is your business or occupation

A. Superintendent of Production.

Q. Are you Superintendent of the Huntington Shore Well at Huntington Beach, California?

A. Yes sir.

Q. How long have you been Superintendent in charge of the Huntington Shore Well?

A. Two years and a half.

(Testimony of Earl Ross.)

Q. And are you familiar with the well known as the Petroleum Well and also known as Fee No. 1 Well at Huntington Beach, California?

A. Yes, sir.

Q. And is that well in the vicinity of the Huntington [227] Shore Well? A. Yes sir. [228]

Q. Do you know if any mud came into the Huntington Shore Well as the result of that redrilling? A. Yes sir.

Q. Do you know how much mud did get into the Huntington Shore Well? A. 3700 feet. [232]

Q. A column of 3700 feet of mud?

A. Yes, 3700 feet of mud.

Q. And what was the effect of that column of 3700 feet of mud on the Huntington Shore Well?

A. It cut off all production and gas, shut the gas off at 7:30 in the morning and at 8:15 we were pumping mud.

The Referee: What date was that?

A. June 8.

Q. This year? A. Yes sir, 1940.

Mr. Rifkind: Q. How long were you shut down?

A. We pumped until 11:00 o'clock and started pulling the tubing and rods out and then we shut down for eleven days.

The Referee: You say 11:00 o'clock in the morning? A. Yes, 11:00 A. M.

Mr. Rifkind: Q. Now, Mr. Ross, how long have you been engaged in the oil business?

(Testimony of Earl Ross.)

A. Since 1915.

Q. 1915. Has your experience been confined to the oil fields of California? A. Yes sir.

Q. How long have you been acting in the capacity of Superintendent?

A. Over four years. [233]

Q. Will you state to the Court what effect or what consequences resulted from the use of mud as a drilling fluid and how it would and did affect the Huntington Shore Well and what the continued use of it might result in doing?

A. Well, it shuts the gas and oil off. We shut the well [236] down for eight days waiting for the casing to be cemented. We then went in to see if there was any mud in the hole and found there was and went on to bale and wash it out, and it went on production on the 26th of June.

The Referee: You put the Huntington Shore Well back on production?

A. We put the Huntington Shore Well back on production on the 26th of June at 10:00 P. M.

Q. Was it necessary for you to do this baling and so forth before you put it on production?

A. Yes.

Q. Explain what you mean by baling?

A. That is how you clean your wells out, you have what you call a baler, two joints of pipe. You go in and bale your well and keep baling it to see if you can clean your mud all out. We cleaned it to the bottom and there was no oil in it. We started

(Testimony of Earl Ross.)

to clean out the perforations and the bit to get the oil to come back.

Mr. Rifkind: Q. Now, if I understand you correctly, as the result of the infiltration of mud through the oil sand and up into the Huntington Shore Well, you were forced to shut down the operation of the Huntington Shore Well on or about June 7, 1940? A. Yes sir.

Q. And you did not resume or were not able to resume operations on the Huntington Shore Well until on or about [237] June 27, 1940?

A. Yes.

Q. Is that correct? A. Yes.

Q. At the time the Huntington Shore Well was forcibly shut down, what was its production?

A. It was doing 265 to 270 barrels a day.

Mr. Rifkind: Q. Now, when the Huntington Shore Well was put back on production on June 27, 1940, what was its production?

A. The first 24 hours was 168 barrels.

Q. Now, between that date what work did you do on the Huntington Shore Well to remove the mud and foreign substances that had come into the well?

A. We were washing and baling.

Q. And did that require labor and material and any apparatus? A. Yes.

Q. State to the Court what you mean by baling and washing?

A. You have to have a crew of four men and a machine to [238] pull your baler. You have a sand

(Testimony of Earl Ross.)

line with a baler and you use your tubing to run your washer in on to clean your perforations out.

Q. As a matter of fact, you alternately wash and bale?

A. Yes, you go in and wash for twenty-four hours and then you go in and bale.

Q. And all during that time your well is off production? A. Yes.

Q. Your tubing and rods have been left out of the well and are on the surface of the ground?

A. Yes.

Q. Or in the derrick rack?

A. Yes. Well, while you are baling and washing you use your tubing.

Q. You say that well was off production for approximately twenty days, is that right?

A. Yes sir.

Q. And that the daily production while that well was shut down was approximately 165 barrels per day?

A. When it first went off it was at 265 barrels per day.

Q. I mean 265.

The Referee: It didn't do anything while it was shut off?

A. Not a thing. For the nineteen or twenty days there was no oil at all.

Mr. Rifkind: Q. Did you get any gas during the twenty days while it was shut down? [239]

A. No.

(Testimony of Earl Ross.)

Q. You lost all the gas? A. Yes.

Q. Do you know what the former income of the wet and dry gas is?

A. No, I don't. I didn't check with Texaco on that.

Q. Now, did you examine the mud which you took out of the Huntington Shore Well and compare it with the mud that was being used by the Bolsa Chica Oil Corporation, or in the re-drilling of the Bolsa Chica Well? A. Yes sir.

Q. And how did they compare?

A. The same.

Q. Well, prior to the re-drilling by the Bolsa Chica Oil Corporation, was there any mud in the Huntington Shore Well? A. No sir.

Q. How much was it cutting?

A. Four to five per cent was the most the well ever cut.

Q. And that was water, was it not?

A. 4.5 is the most it ever cut before of water.

Q. And none of that cut was mud or sand?

A. No sir.

Q. Or anything like that. Now, Mr. Ross, what effect did this mud have upon the tubing and rods of the Huntington Shore Well, or what effect would the continued use of mud as [240] a re-drilling fluid by the Bolsa Chica Oil Corporation have upon the tubing and rods and pump of the Huntington Shore Well?

(Testimony of Earl Ross.)

A. Why, if we had mud in it would ruin it. They would not be no good.

Q. In other words, as long as the Bolsa Chica Well continued to use mud the Huntington Shore Well cannot operate?

A. Not if it is in the same channel.

Q. And have you in your experience known of wells which have been completely lost by reason of freezing and clogging due to the use or seepage of mud as a drilling fluid? A. Some, yes.

Q. Mud, when used as a drilling fluid, is in liquid form? A. Yes.

Q. And it accumulates a certain amount of what is commonly known as cuttings? A. Yes.

Q. And sand? A. Yes.

Q. And other foreign substances?

A. Yes.

Q. And the mud carries those foreign substances through the oil sands up and into the well?

A. Yes.

Q. And those foreign substances work between the tubing and rods and get into the pump, is that correct? [241] A. That is it.

Q. Now, these oil sands, are they porous?

A. Yes, they channel. [242]

Q. Now, Mr. Ross, when this mud infiltrates and passes through the porous oil sands you have mentioned, does a certain amount of it settle and harden in the oil sand?

(Testimony of Earl Ross.)

A. A certain amount hardens and packs in and shuts it off.

Q. When the mud with its cuttings and sand and other foreign substances gets into the adjoining well which is on production, doesn't a certain amount settle to the bottom and cling to the sides and clog up the tubing and rods in operation?

A. Yes sir.

Q. In other words, while the mud is in liquid form in the process of re-drilling it solidifies when it leaves the well that is being re-drilled, is that it? A. Yes sir. [243]

Cross Examination

By Mr. Pallette:

Q. I believe you testified, Mr. Ross, that the oil comes into the hole through channels in the sands?

A. Yes. [252]

Q. Your well was on the pump on the 8th day of June, along in that time? A. Yes sir.

Q. And the oil is sucked out of the hole through these channels into the hole and through the action of the plunger of the pump? A. Yes sir.

Q. Did you shut down your well or was your well shut down at the time the mud appeared inside the hole? A. No sir.

Q. Or was it pumping? A. Pumping.

Mr. Pallette: That is all. [253]

Q. And when you say the Bolsa Chica Well lost circulation and the Huntington Shore gained it, the

(Testimony of Earl Ross.)

circulation disappeared from the Bolsa Chica Well and came in the Huntington Shore Well?

A. Yes sir.

Q. And at the time that took place was there any mud of any kind being used on the Huntington Shore Well? A. No sir.

Q. And the minute that mud appeared it started to affect the operations of the Huntington Shore Well? A. Yes.

Q. And pretty soon you had no oil at all in the well? A. No oil, and pumping mud.

Q. You say Mr. Anderson told you they lost circulation at 4413 feet. From your experience in the Huntington Beach field, do you know whether 4413 feet is a part of the producing-oil zone in the Huntington Beach oil field?

A. It is at the top strata of the gas zone.

Q. It is a part of the oil zone?

A. Yes. [254]

VERNON KING,

called as a witness on behalf of the Trustee, being first duly sworn, testified as follows:

The Referee: Give your full name to the reporter? A. Vernon King.

Q. And your address?

A. 401 Haas Building.

The Referee: You may proceed.

[Testimony of Vernon King.)

Direct Examination

By Mr. Dechter:

Q. What is your occupation or profession?

A. Petroleum geologist and engineer.

Q. Are you a graduate of any school in which you majored in geology or petroleum engineering?

A. Yes sir.

Q. What university? A. Stanford.

Q. How long have you been engaged as a geologist and petroleum engineer? A. Since 1919.

Q. How long have you been practicing that profession in California? A. Since that time.

Q. Are you familiar with the Huntington Shore oil field? A. I am. [256]

Q. How long have you been engaged as a petroleum engineer and geologist in the Huntington Beach oil field?

A. The first well there was in 1920 or '21; 1921, I think.

Q. You have been engaged there continuously?

A. No, intermittently.

Q. Are you also familiar with the portion of the Huntington Beach field which is called the tideland area? A. I am.

Q. How long have you been engaged in that particular area?

A. Since,—roughly, since 1932. I think it was discovered about that time.

[Testimony of Vernon King.)

Q. Are you familiar with the Huntington Shore Well?

A. I am. I am familiar with the re-drilling of it since 1937.

Q. In other words, you have been acting as petroleum engineer on the Huntington Shore Well from the time it was re-drilled in 1937?

A. Yes, I was the engineer on the well at the time it was re-drilled in 1937.

Q. Have you been employed by the State of California as Consulting Engineer in connection with the Huntington Beach area? [257]

A. Well, I am not employed by them. I am on their consulting staff.

Q. I see. Are you familiar with the Bolsa Chica Petroleum Fee Well?

A. I am generally familiar with the operations carried on there in June.

Q. You are also familiar with the general area in the Huntington Beach field? A. Yes.

Q. And the wells producing therefrom. In other words, you have had access to the drilling records and production records?

A. Access and examination of the completed data, and have worked on a good many of the wells as engineer.

Q. You have made an examination and analysis of the surveys, plats, courses and charts on file with the Division of Lands of the State of California

[Testimony of Vernon King.)

showing the costs of the Petroleum Well at Huntington Beach, California? A. I have.

Q. You are also familiar with the nature of the stratigraphy, as it is termed, of the oil sands in the Huntington Beach area? A. Yes sir.

Q. Were you employed as petroleum engineer of the Huntington Shore Well on or about June of 1940 when a column of mud appeared in the Huntington Shore Well while it was on [258] production and pumping oil? A. I was.

Q. Will you please state to the Court just what you observed as the result of your investigation?

A. Briefly, the Huntington Shore Well was on steady production and had been for a number of years producing at the rate of variously from 275 to 300 barrels per day. It was pumping at that rate. The well suddenly failed—producing both oil and gas, and the well suddenly, on about June 8, shut off the gas or the gas stopped coming in and in about an hour and a half started to produce pure mud. Within a couple of hours a pulling unit had arrived and the rods and tubing pulled out and we found the mud was up to about 1900 feet from the surface, or about 3700 feet of mud.

Q. In other words, a column of mud extending from the bottom of the hole up 3700 feet?

A. Yes, up to the casing. That is the measured depth of the hole.

[Testimony of Vernon King.)

Q. What would have happened to the tubing and rods if the tubing and rods had not been removed within an hour after that mud was discovered in the well?

A. Generally they stick. You don't pull them out.

Q. If the tubing and rods should be frozen, as the expression is used, by the hardening of the mud that infiltrated into the Huntington Shore Well, what would have happened to the Huntington Shore Well? [259]

A. Anything from a fishing job to an abandonment of the well, depending on how much of that mud could get out or whether you could get it all out.

Q. Would you say there was grave danger of the well being lost by reason of the infiltration of mud? A. Yes, there is always a danger. [260]

Q. And calling your attention to the point at 4413 feet where the Bolsa Chica Petroleum Fee Well enters the oil sand can you tell us what distance the bottom of the Bolsa Chica Well at that depth was from the producing oil sands of the Huntington Shore Well?

A. The well was approximately scaled on the surface, scaled about 110 feet from the casing of the Huntington Shore Well. That casing, however, is blank down a couple of hundred feet below that, I should say roughly 110 feet apart, and in the

[Testimony of Vernon King.)

hole the mud would probably travel another 150 or [261] 200 feet in the casing to get into the hole. It would be a right-angle bend there. [262]

Q. What was the effect of the infiltration of this column of mud, 3700 feet high, in the Huntington Shore Well on the production of oil from the Huntington Shore Well?

A. It absolutely cut it off. There was no production at all either of oil or gas.

Q. And what was necessary to be done to bring the Huntington Shore Well back on production after that occurred?

A. It was necessary to clean that mud out and that was done by alternately baling and washing.

Q. Are you able to estimate the expense the Huntington Shore Well was put to in replacing the Huntington Shore Well on production?

A. The actual baling and cleaning operations took some twenty days, something over—about thirty-two to thirty-five hundred dollars. Then there was a loss of oil there for those twenty days which would amount to about 6,000 barrels of oil. The market price was ninety cents.

Q. Was there any permanent effect on the amount the Huntington Shore Well was capable of producing after this [264] mud had entered and after the well had been cleaned out and placed on production again?

[Testimony of Vernon King.)

A. Yes, the well after two months is making fifty to seventy-five barrels less than it did before, and making less gas than it did before.

Q. And in your opinion is that decrease in the production of oil and gas in any wise chargeable to the infiltration of mud in the Huntington Shore Well? A. I believe it is.

Q. Isn't it a fact that mud has a tendency to shut off the oil channels which have been constantly piling and widening and opening?

A. Once sand is mudded up there are certain physical conditions that govern the removal of that sand and mud. We do not always understand exactly what they are and sometimes when we do we cannot correct them, but it generally happens once a well has been mudded off, especially a well that has been producing, some rejuvenation of that well, or complete rejuvenation of that well, is not possible. **[265]**

[Testimony of Vernon King.)

(TRUSTEE'S EXHIBIT NO. 1)

Hubert F. Laugharn
Trustee in Bankruptcy in the Matter of
Jack Dave Sterling, Bankrupt.

September 26, 1940

To

Bolsa Chica Oil Corporation

In re: Huntington Shore Well, Huntington Beach, Calif.

Loss of production of oil for 20 days, June 7 to June 27, 1940, 265 barrels per day at 90¢ per barrel	$ 4,770.00
Loss of production of wet and dry gas, June 7 to June 27, 1940, 20 days	248.00
Loss of production of oil as result of reduction in output, June 27 to Sept. 1, 1940, 3,700 barrels @ 90¢	3,330.00
Loss of production of wet and dry gas as result of decline, June 27 to Sept. 1, 1940	550.00
Pulling, baling, washing and other materials, labor and technical assistance in removing mud, sand and other foreign substances	3,642.00
	$12,540.00

[Endorsed]: Trustee's Exhibit No. 1. Filed Sept. 26, 1940. Ernest R. Utley, Referee.

[Endorsed]: Filed Dec. 31, 1940. R. S. Zimmerman, Clerk. [96]

Mr. Dechter: Q. Mr. King, did you prior to June 7, 1940, give your consent in writing to the Bolsa Chica Corporation for the use of drilling

[Testimony of Vernon King.)

mud in their Bolsa Chica Well? A. No sir.

Q. Did you at any time prior to June 7, 1940 verbally give your consent to their using drilling mud in their well?

A. In using drilling mud in their oil sand?

Q. In other words, calling your attention to the language of the order for injunction, did you at any time give your consent to use anything other than crude oil while drilling in the oil sand?

A. No. At each time the question came up it had come up of course there was to be virgin crude oil to be used in the [269] oil sand. [270]

Cross Examination

By Mr. Pallette:

Q. I believe you testified you at no time gave your consent to drilling with anything except virgin crude oil in the oil sand? A. Yes.

Mr. Dechter: To which we object as incompetent unless the consent had been in writing and the writing is exhibited to the witness, the order for injunction calling for consent in writing.

The Referee: Objection overruled.

The Reporter: "Yes."

Mr. Pallette: Q. I take it from the fact you limited your answer to the oil sand that you did consent to the use of mud above the oil sand, that is in the shale body?

Mr. Dechter: To which we object as immaterial. All the respondents are being charged with is using

[Testimony of Vernon King.)

drilling mud in the oil sand in violation of that portion of the injunction which requires them to use virgin crude oil.

Mr. Cree: If that is the case—well, go ahead.

Mr. Pallette: Your objection then is to the use of mud in the oil sand?

Mr. Dechter: That is right.

Mr. Pallette: And that is all?

Mr. Dechter: In the oil zone. I want to retract that statement. Mr. Rifkind calls my attention to the fact the [272] injunction is broader than that, and I will withdraw my objection.

The Referee: The objection to the question is overruled. Read the question.

(The reporter read the pending question as follows:

"Q. I take it from the fact you limited your answer to the oil sand that you did consent to the use of mud above the oil sand, that is in the shale body?")

A. I was naturally at the well considerably, a several number of times and in discussing those things I referred them that I was under, working under the injunction and that I could not except by writing do or give them consent to use mud in the oil zone.

Mr. Pallette: You mean in the oil zone?

A. In the oil zone, yes, and since the mud was discussed previous to the time or during the time the injunction was being sought. That was understood by both parties.

[Testimony of Vernon King.)

Mr. Pallette: Will you read that answer?

(The reporter read as requested.)

The Referee: Do I understand by that answer you never at any time gave any consent in writing to use mud?

A. No. It was recognized by all parties mud was being used until they reached the oil sand. Naturally, they being the oil operators, it was incumbent on them to tell just when they entered that zone.

The Referee: But you did not give them consent yourself? [273]

A. No, no.

Mr. Pallette: Q. It is true, Mr. King, that you were at the well, I won't say every day but several days a week during the proceedings?

A. Yes.

Q. And that all records and operations were made available to you during that time by the operators of the Bolsa Chica Well?

A. I think all of them.

Q. And all that you asked for? A. Yes.

Q. You were familiar with the fact that immediately after circulation was lost it was necessary for the Bolsa Chica to go back into the hole with a mixture of Aquajel in order to restore circulation?

A. Yes.

Q. And you were present at the well during those operations? A. I was.

Q. And did you at any time discuss with Mr. Anderson or Mr. Nichols what they were proposing

[Testimony of Vernon King.)

to do at that time and how they were going to do it?

A. Why yes. We had a number of discussions on it and naturally wanted to be helpful and for that reason we closed our well in for eight days so that they might complete their operations even after they had mudded our well up. [274]

Q. That is, completing their job by the use of mud and Aquajel to restore the necessary circulation? A. Yes.

Q. You knew in running their casing it was necessary to restore circulation and in so doing they were going to use mud and the mixture of Aquajel?

A. Yes.

Q. You are also familiar with the fact that from that time on for about approximately forty-five days they continued to drill with mud?

A. In different holes. They had several different holes there.

Q. In other words, I will reframe the question—

A. Above the oil zone. They were above the oil sand most of the time.

Q. They did not approach the oil sand again until the latter part of July, and from the 8th of June until the latter part of July they were not in the oil sand and at all times were drilling with mud with your knowledge and consent?

Mr. Dechter: To which we object on the ground it is incompetent, irrelevant and immaterial. This witness would have no right to give any consent except by a document in writing.

[Testimony of Vernon King.)

The Referee: Objection sustained.

Mr. Pallette: May it please the Court, with reference to your ruling on that objection if I may make a statement [275] with reference to it?

The Referee: Very well.

Mr. Pallette: At the time this injunction was agreed to we had a conference between the engineers here during the afternoon, if you will recall, which was solely with reference to the direction and course of the well. The engineers eventually agreed on a course that was satisfactory. We then started to draft the form of the order, Mr. Rifkind did, and he suddenly said that he wanted a provision there with reference to the use of a circulating medium restricting it to oil, which was completely outside of any argument which had taken place up to that time. Mr. King was present, Mr. Templeton, Mr. Anderson and Mr. Jussen. As I recall the conversation was to the effect that if we would agree to a clause being inserted in the injunction to the effect we would not use anything but oil except with Mr. King's consent, that we would have no difficulty if something unforeseen came up if we had to use mud, that they were sure the engineers could get together on it and work it out without any trouble. The provision as to the writing was put in by Mr. Rifkind without any discussion, purely as I saw it as a matter of evidence, something to evidence that consent. It does not go to the fact of the matter that what we were doing was to be subject at all

[Testimony of Vernon King.)

times to the supervision and control of Mr. King, but if something came up, we had to back up to cement he was to have supervision [276] over that. If it turned out there was some circulating medium better than oil, and there was considerable discussion about the Shell patented medium which might be better, our engineer was to get together with him and everybody was sure there would no difficulty. The main argument was about the course, and we did not consider there would be any question at all about,—any serious question arise as to the use of mud which could not be settled between the engineers.

Subsequently, it turned out we could not use oil in our operations in the shale. It is my understanding that Mr. King was contacted, that our engineer did not understand at the time it was necessary to get his consent in writing, that he conferred at all times with reference to what he was going to do with Mr. King, that Mr. King had knowledge of what was going on for a period of approximately forty-five days.

The Referee: Isn't that a matter of defense on the part of the respondents to the order to show cause rather than on the affirmative?

Mr. Pallette: Well, on direct here it was brought out he at no time consented in writing to the use of mud. I am merely trying to bring out he did consent to the use of mud in the shale body and at no time saw any objection to the use of mud in the shale body until the 31st of July and for a

[Testimony of Vernon King.)

period of approximately two months with the knowledge and [277] oral consent of Mr. King we in good faith proceeded to drill in the shale body, and when he eventually requested us to change to oil when we got to the oil body we did change to oil.

Mr. Dechter: If counsel's statement is a statement in the nature of an offer of proof we object as incompetent and as being a collateral attempt to impeach an order which has now become final, and the only way of securing relief from this order is by making an application to the Court. [278]

The Referee: I think I will let my ruling stand as made, and if you intend the statement just made as an offer of proof I will sustain the objection to it. [279]

(TRUSTEE'S EXHIBIT No. 2)

July 31, 1940.

Bolsa Chica Oil Corporation,
555 South Flower Street,
Los Angeles, California

Gentlemen:

An Injunction against the Bolsa Chica Oil Corporation was issued In the Matter of Jack Dave Sterling, Bankrupt, District Court of the United States, Southern District of California, Southern Division, In Bankruptcy No. 26685-Y, on May 15, 1940, enjoining the Bolsa Chica Oil Corporation, its superintendent, agents and employees from using mud as a circulating fluid in the redrilling of its "Fee No. 1 Well" at Huntington Beach, California.

We have been informed that despite said injunction and wthout our consent and in direct refusal of our consent you are using mud as a circulating fluid in the redrilling of said well.

This is to notify you that unless you forthwith desist using mud as the circulating fluid in the redrilling of said well that an application will be made to the United States District Court to have you cited and punished for contempt for violating said injunction aforesaid.

Yours truly,
JOSEPH J. RIFKIND and
RAPHAEL DECHTER
By JOSEPH J. RIFKIND
Attorneys for Hubert F. Laugharn, as Trustee in Bankruptcy of Jack Dave Sterling, Bankrupt.

JJR:S

c/c Bolsa Chica Oil Corporation
Huntington Beach, California — Spec. Del.
Attn: Mr. Anderson, Superintendent — Reg.
RRR

Overton, Lyman & Plumb,
Attn: Mr. Pallette. (blind)
Dechter
Laugharn
Sterling
King

(Receipts for Registered Articles Nos. 352963 and 352964 attached.)

(Return Receipts dated August 1, 1940 and signed by Bolsa Chica Oil Corp. by Mrs. Jr. Nichols and By Bolsa Chica Oil Corp. by John W. Deichman attached)

[Endorsed]: Tr. Exhibit No. 2 (4 documents). Filed September 26, 1940. Ernest R. Utley, Referee.

(TRUSTEE'S EXHIBIT No. 3)

DRILLING AND OPERATING AGREEMENT

This agreement, made and entered into this 14th day of August, 1940,

By and between

Bolsa Chica Oil Corporation, a corporation, as First Party, hereinafter called

"Bolsa Chica",

and

M. M. McCallen Corporation, a corporation, as Second Party, hereinafter called

"McCallen".

Witnesseth:

That whereas, concurrently herewith Bolsa Chica has assigned to McCallen that certain Oil and Gas Lease, and the leasehold thereby created, made and entered into on the 20th day of February, 1940, by and between The Petroleum Company, a corporation, as Lessor, and Bolsa Chica Oil Corporation, as Lessee, covering and demising the following described real property, to-wit:

Lots Twenty (20) and Twenty-two (22), Block One Hundred Nineteen (119), in the City of Huntington Beach, County of Orange, State of California, as per map recorded in Book 4, Page 10 of Maps, Miscellaneous Records of said Orange County,

which said assignment is absolute in form but is, in truth and in fact, made subject to the agreements and conditions hereinafter set forth in this Agreement; [97]

And whereas, the parties hereto desire to and do hereinafter set forth the agreements and conditions upon which and subject to which said absolute assignment is made,

Now, therefore, the parties hereto do agree as follows:

1. Bolsa Chica hereby gives and grants to McCallen the right to take possession of the herein premises, together with the idle oil well now located thereon and the equipment appurenant thereto, including all drilling equipment, casing, cement, oil, mud, bits, etc., now therein and thereon, with the right to use all such equipment and personal property, free of cost, in the reconditioning, redrilling and placing on production of the said well as a producing oil well, and together with the right thereafter to produce the said premises, all upon the terms and conditions hereinafter set out. McCallen agrees, at all times that it is in possession of the herein premises, to faithfully perform the agreements and observe the conditions in the Oil and Gas

Lease demising the herein premises, or the leasehold thereon, except as in this Agreement otherwise provided. McCallen further agrees to immediately commence operations in and on the said well now standing idle on the herein premises and to thereafter carry on such operations without interruption, until such time as said well has been placed on production as a producing oil and gas well or until such time as the herein premises are reconveyed to Bolsa Chica. In this connection, it is understood that if McCallen fails, within a period of forty-five (45) days to complete its drilling and reconditioning operations hereunder, its rights to the herein premises shall cease and terminate and it shall then be under obligation to reconvey the said premises to Bolsa Chica, free of any claim hereunder thereto; and McCallen agrees so to do. [98]

2. If, as, when and after the herein premises are, by the efforts of McCallen hereunder, made to produce oil, gas and/or other hydrocarbon substances, it is understood that the proceeds realized from the sale of all such production shall be disbursed by McCallen as follows:

First: All federal, state, county and municipal taxes, assessments for the production fund of the State and any other taxes, assessments or levies which must be paid on account of the discovery or production of oil, gas and other hydrocarbon substances on or from the herein premises, whether assessed upon the land, or as mineral rights, severance taxes, or otherwise.

Personal property taxes, however, shall be paid by McCallen out of the operating allowance agreed to in sub-paragraph Fourth of this paragraph.

Second: Fifteen per cent. (15%) of the balance of such proceeds shall be paid to the Lessor and/or assigns of the Lessor named in the Lease demising the herein premises and owning the landowner's or Lessor's royalty, all as agreed in the original Lease demising the herein premises.

Third: All compensating royalties payable to the State of California, and all expenses incurred incidental to obtaining and carrying out the provisions of the compensating royalty agreements and the fees and expenses payable to the Huntington Beach Townsite Association in connection with the maintenance and operation of the herein well.

Fourth: Then, out of the remaining proceeds, McCallen shall, each month, retain, for the operation, maintenance and repair of the herein well, during the productive life thereof, the actual costs and expenses thereof, together with the excess, if any, over the said actual costs and expenses caused by the expense of dehydrating the oil produced.

Fifth: The money remaining each month, after making the payments in the preceding sub-paragraphs of this Paragraph 2, shall be retained or paid by McCallen as follows:

(a) Eighty per cent. (80%) thereof shall be retained by McCallen until such time as it has been thereby repaid all costs and expenses incurred by it in and about its operations hereunder in reconditioning, redrilling and placing on production of the herein well.

(b) The balance, or twenty per cent. (20%) thereof, shall be paid to Bolsa Chica until such time as McCallen has been reimbursed as just hereinabove set out. [99]

Sixth: The money remaining each month, after all the foregoing payments have been made and reimbursements had, shall be retained or paid by McCallen, as follows:

(a) Eighty per cent. (80%) thereof shall be paid to Bolsa Chica until such time as Bolsa Chica has been thereby paid the sum of Forty Thousand Dollars ($40,000.00). In this connection, it is understood that the money theretofore paid to it by McCallen, as agreed in sub-paragraph Fifth hereof, shall be a credit to McCallen toward the payment of said sum of Forty Thousand Dollars ($40,000.00).

(b) The balance, or twenty per cent. (20%) thereof, shall be retained by McCallen until such time as Bolsa Chica has been paid the sum of Forty Thousand Dollars ($40,000.00), as just hereinabove set out.

Seventh: After all the payments have been made and the reimbursements had, as set forth in all of the foregoing sub-paragraphs of this Paragraph 2, McCallen shall, each month, during the remainder of the life of the herein well, pay one-half (½) of such remaining money to Bolsa Chica and shall retain the remaining one-half thereof.

All payments herein made shall be made on or before the 25th day of each month for oil and gas produced, saved and sold during the preceding calendar month.

3. The costs and expenses of reconditioning, redrilling and otherwise working in and about the herein well and placing the said well on production, shall include all payroll expense, compensation and other necessary insurance carried, costs of all materials and supplies and other personal property used, including bits, welding, cement, cementing, rentals and every other thing used or service required in and about such operations of McCallen hereunder.

4. McCallen shall, at any time hereafter, have the right to abandon operations on the herein well, and thereupon all rights and obligations of each party to the other shall cease and terminate; and upon such abandonment, McCallen shall have the right to remove from the premises the equipment placed therein and thereon by it. [100]

5. Title to all oil well drilling and producing equipment and personal property in, on and about the herein premises and the well hole thereof, shall remain in Bolsa Chica until such time as Bolsa Chica has been paid the sum of Forty Thousand Dollars ($40,000.00), as hereinabove set forth. Thereafter, such equipment shall be owned by the parties hereto in equal undivided parts. It is agreed, however, that all drilling and other miscellaneous equipment not necessary for use in producing said well, now owned by Bolsa Chica and in and on said well, shall, at the termination of its use by McCallen be returned at the well site to Bolsa Chica for removal by it.

6. Bolsa Chica may, at all reasonable times, examine the herein premises, the work done and in progress thereon, and the production therefrom, and may inspect the books of account kept by McCallen in relation to the production from said well and the costs and expenses of all operations carried on by McCallen hereunder.

7. McCallen shall, at all times hereafter, have the absolute management, control and direction of all drilling and producing operations on the herein premises.

Nothing herein contained shall be considered as making the parties hereto partners, joint adventurers, or associates of any kind, it being the intention of the parties hereto that the only interest of Bolsa Chica hereunder shall be its right to be paid

by McCallen the proceeds from production of the herein well, as hereinabove agreed, as consideration for the assignment of the herein Lease, leasehold and well.

8. In the event commercial production is obtained from said well, Bolsa Chica agrees to pay the Four Thousand Dollars ($4,000.00) cash payment for the purchase price of certain personal property on said premises, as set forth in [101] Paragraph 16 of the above mentioned Oil and Gas Lease of February 20, 1940, and shall have no right to reimbursement therefor hereunder as against McCallen. In short, it is understood that the whole of said Four Thousand Dollars ($4,000.00) shall be paid by Bolsa Chica outside the agreements herein contained.

9. This Drilling and Operating Agreement shall not be assigned, in whole or in part, by McCallen without the written consent of Bolsa Chica first obtained, and the herein premises shall not be underlet or sublet, in whole or in part, without the like written consent of Bolsa Chica first obtained.

10. This agreement shall be binding upon and inure to the benefit of the heirs, executors, administrators, successors and assigns of the parties hereto.

It witness whereof, the parties hereto have caused this Agreement to be executed by their respective duly authorized officers, and their respective cor-

porate seals to be hereunto affixed, all as of the day and year first hereinabove written.

BOLSA CHICA OIL
[Corporate Seal] CORPORATION
By THOS. W. SIMMONS
President
By W. S. PALLETTE
Secretary
"First Party — Bolsa Chica"
M. M. McCALLEN
CORPORATION
By H. H. McVICAR
President
By C. M. ROOD
Secretary
"Second Party — McCallen"

[102]

State of California
County of Los Angeles—ss.

On this 14th day of August, 1940, before me, the undersigned, a Notary Public in and for said County and State, personally appeared Thos. W. Simmons, known to me to be the President, and W. S. Pallette, known to me to be the Secretary of Bolsa Chica Oil Corporation, the corporation that executed the within Instrument, known to me to be the persons who executed the within Instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

Witness my hand and official seal.

[Seal] GERTRUDE M. KNIGHT

Notary Public in and for the County of Los Angeles, State of California.

My Commission expires July 20, 1942.

State of California
County of .....—ss.

On this .....day of August, 1940, before me, the undersigned, a Notary Public in and for said County and State, personally appeared....., known to me to be the President, and....., known to me to be the Secretary of M. M. McCallen Corporation, the corporation that executed the within Instrument, known to me to be the persons who executed the within Instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

It witness whereof, I have hereunto set my hand and affixed my official seal the day and year in this Certificate first above written.

.....

Notary Public in and for said County and State.

[Endorsed]: Trustee's Exhibit No. 3. Filed Sept. 26, 1940, Ernest R. Utley, Referee.

[Endorsed]: Filed Dec. 31, 1940, R. S. Zimmerman, Clerk. [103]

(TRUSTEE'S EXHIBIT No. 4)

ASSIGNMENT OF OIL AND GAS LEASE

Know all men by these presents:

That Bolsa Chica Oil Corporation, a corporation, for and in consideration of the sum of Ten Dollars ($10.00) to it in hand paid, receipt of which is hereby acknowledged, does hereby sell, assign, transfer and set over unto M. M. McCallen Corporation, a corporation, that certain Oil and Gas Lease, and the leasehold thereby created, made and entered into on the 20th day of February, 1940, by and between The Petroleum Company, a corporation, as Lessor, and Bolsa Chica Oil Corporation, a corporation, as Lessee, covering and demising the following described real property, to-wit:

> Lots Twenty (20) and Twenty-two (22), Block One Hundred Nineteen (119), in the City of Huntington Beach, County of Orange, State of California, as per map recorded in Book 4, Page 10 Maps, Miscellaneous Records of said Orange County,

To have and to hold unto the said M. M. McCallen Corporation, a corporation, forever during the remainder of the life of said Oil and Gas Lease of February 20, 1940.

It witness whereof, the Assignor herein has caused this Assignment to be executed by its duly authorized officers and its corporate seal to be here-

unto affixed, all as of this 14th day of August, 1940.

BOLSA CHICA OIL
[Corporate Seal] CORPORATION
By THOS. W. SIMMONS
President
By W. S. PALLETTE
Secretary [104]

State of California
County of Los Angeles—ss.

On this 14th day of August, 1940, before me, the undersigned, a Notary Public in and for said County and State, personally appeared Thos. W. Simmons, known to me to be the President, and W. S. Pallette, known to me to be the Secretary of Bolsa Chica Oil Corporation, the corporation that executed the within Instrument, known to me to be the persons who executed the within Instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

It witness whereof, I have hereunto set my hand and affixed my official seal the day and year in this Certificate first above written.

[Notarial Seal] GERTRUDE M. KNIGHT
Notary Public in and for the County of Los Angeles, State of California.

My Commission expires July 20, 1942.

[Endorsed]: Trustee's Exhibit No. 4. Filed Sept. 26, 1940, Ernest R. Utley, Referee.

[Endorsed]: Filed Dec. 31, 1940, R. S. Zimmerman, Clerk. [105]

(TRUSTEE'S EXHIBIT NO. 6)

August 21, 1940

McVicar-Rood, Inc.
Huntington Beach,
California

Gentlemen:

Hubert F. Laugharn, as Trustee in Bankruptcy of Jack Dave Sterling, Bankrupt, has been informed that the Bolsa Chica Oil Corporation has or proposes to assign its oil and gas lease covering or enter into an agreement with you respecting its "Petroleum Well", also know as "Fee No. 1 Well", at Huntington Beach, California.

The Trustee in Bankruptcy hereby directs your attention to the fact that an injunction against the Bolsa Chica Oil Corporation was issued In the Matter of Jack Dave Sterling, Bankrupt, District Court of the United States, Southern District of California, Central Division, In Bankruptcy No. 26685-Y, on May 15, 1940, prohibiting the redrilling of said "Petroleum Well", also known as "Fee No. 1 Well", closer than 200 feet from the "Huntington Shore Well" of said bankrupt estate, measured on a horizontal plane, at any point beneath the depth of 3800 feet below sea level, and further providing that the circulating fluid used in the drilling, redrilling or sidetracking of said "Petroleum Well", also known as "Fee No. 1 Well", shall be virgin crude oil, and that no mud or other foreign substances shall be used as a circulating fluid.

A certified copy of the Injunction against the Bolsa Chica Oil Corporation is herewith enclosed for your formal notice. It is the Trustee in Bankruptcy's position that the Bolsa Chica Oil Corporation's assigns and successors are bound by said injunction. See Lake v. Superior Court, 165 Cal. 182.

Yours truly,

JOSEPH J. RIFKIND

JJR:S

Enc.

c/c Division of Oil and Gas,
State of California
629 South Hill Street,
Los Angeles, California

Division of Lands,
State of California,
State Building,
Los Angeles, California

c/c Hubert F. Laugharn, Esq. (blind)
Vernon L. King, Esq. "
J. D. Sterling, Esq. "
Raphael Dechter, Esq. "

Return receipt dated Aug. 22, 1940 signed by McVicar-Rood, Inc. attached.

[Endorsed]: Tr. Exhibit No. 6. Filed Sept. 26, 1940. Ernest R. Utley, Referee.

JACK DAVE STERLING,

called as a witness on behalf of the Trustee, being first duly sworn, testified as follows:

The Referee: Give your full name to the reporter.

A. Jack Dave Sterling.

Direct Examination

Mr. Dechter:

Q. What is your business, Mr. Sterling?

A. Oil operator.

Q. How long have you been so engaged?

A. Since 1928.

Q. Have those operations been confined to California? A. Yes sir.

Q. During your experience as oil operator how many wells [357] have you drilled or been interested in? A. Twenty-two.

Q. Where have those wells been located?

A. They have been located in Long Beach, Huntington Beach, the Torrance field and Bakersfield.

Q. Are you familiar with the Huntington Shore Well? A. I am.

Q. You were the one who originally drilled the Huntington Shore Well? A. Yes sir.

Q. Are you familiar with what happened in the Huntington Shore Well in 1937 when it became necessary to re-drill the same? A. I am.

Q. Will you state to the Court just what took place at that time?

(Testimony of Jack Dave Sterling.)

A. In 1937—I don't know if I got the question right. In re-drilling the well?

Q. What took place before it became necessary to re-drill the well, if you know?

A. In 1937 the well was drilled by the Termo Oil Company and they used some cement in plugging the hole——

The Referee: You are telling now what happened to cause a re-drilling of the well?

A. That is right, your Honor. And cement caused to stick the tubing in the Huntington Shore Well which is called a [358] fishing job, and we were unsuccessful in fishing tools out and therefore we had to re-drill the well.

Mr. Dechter: Q. In other words, this cement came from the Termo Well that at that time was drilled at or about the same depth as the Huntington Shore Well? A. Yes sir.

Q. And caused your tubing and rods to be stuck in the hole? A. That is right.

Q. And were you able to remove the tubing and rods?

A. There wasn't any rods in the hole. It was a flowing well.

Q. I see.

A. There was tubing in there, part of it we recovered and part left in the hole.

Q. What happened to the original hole by reason of cement coming in?

(Testimony of Jack Dave Sterling.)

A. We had to plug it off or re-drill it.

Q. When you say you had to plug it off, or re-drill it, do you mean you could use the original hole? A. Part of it.

Q. How much of it?

A. About forty-two hundred feet.

Q. And what did it cost you to re-drill that hole?

A. It cost us about $80,000 plus twenty per cent.

Q. And would the entrance of mud from an adjacent drilling [359] well have the same effect on your tubing as cement?

A. There is no question about it.

Q. In other words, cement in the drilling well is in fluid or working condition just as drilling mud? A. That is right.

Q. And after it loses its water it hardens, and mud would harden the same as cement?

A. That is right.

Q. Were you the one who re-drilled this well for the Trustee at a cost of $80,000? A. I did.

Q. Now, calling your attention to June 7. Are you familiar with what happened to the Huntington Well on that particular date? A. I am.

Q. Will you state to the Court just what you know about it?

A. In the morning Mr. Ross, he is Superintendent of the well in Huntington Beach, he called me and told me that the well started pumping mud so I immediately went over to Huntington Beach

(Testimony of Jack Dave Sterling.)

and I instructed him immediately to pull the tubing and the rods from the well in order not to stick the tubing and rods in the well so we would not have a similar job as we did in 1937 when the cement came through from the Termo Well. Immediately I went over to the Bolsa Chica Well and we found that they have lost mud. We taken a [360] sample of the mud that they lost and also taken samples of the mud we have received in the Huntington Shore Well.

The Referee: You say you took a sample of the mud that they lost. You mean you took a sample of mud at their well?

A. At their well and in the ditch and also a sample of the mud we received.

Mr. Dechter: Q. You took a sample of the mud at the Huntington Shore Well and at the Bolsa Chica Well, and did you observe whether they were the same or whether they were different?

A. The same mud.

Q. What else did you do at that particular time?

A. I instructed Mr. Ross to leave the well after pulling the tubing to stand until such time as they finished their well and he carried out my instructions.

Q. What happened after that?

A. In about twenty days later they have quit operating or doing any work on the well so we went in the hole and we found about thirty-five

(Testimony of Jack Dave Sterling.)

hundred feet of mud in the hole, and we started baling and washing out. After baling for about two days and cleaning out the hole we found there wasn't any oil, and after that we started washing the perforations to bring in the oil, which we did, and finally in a couple of days started to get the oil in after pumping the well two or three days finally putting it back on the same stroke as we had before the well went off. We found the best production [361] we can get is about 215 barrels, maximum production.

Q. And what was your average production before the well was mudded off?

A. Between 285 to 300 barrels.

Q. In other words, there was a loss, a permanent loss of about 75 barrels a day?

A. There is a permanent loss I would say of from 60 to 75 barrels a day.

Q. Do you have an opinion as an experienced oil driller and operator as to what caused the Huntington Shore Well to be mudded off?

A. Well, their hole was so close to this hole and when they broke circulation in their hole that caused the mud to come through into the Shore Well and mudded off.

Q. You testified before this Court on the hearing leading up to the injunction against the Bolsa Chica Oil Corporation?

(Testimony of Jack Dave Sterling.)

A. I did, and I stated in this court that that thing would happen before they even commenced drilling.

Q. In other words, you gave it as your opinion to the Court before the injunction was issued that if they used mud that is what would happen to the Huntington Shore Well? A. Yes sir.

Q. Will you state to the Court what would have happened if you had not maintained a constant vigilance on the Huntington Shore Well?

A. I am sure we would have another fishing job, a [362] re-drilling job.

Q. In other words, a similar experience to what you had in 1937?

A. Yes sir, correct. [363]

ALLAN A. ANDERSON

Direct Examination

Q. Would you state what happened in connection with the well on or about the 19th day of May, 1940?

A. Why, sometime after the middle of July—of May, I should say it was, we decided from our experience in encountering the lower portion of the hole that it would be impractical to attempt to complete the well from that particular location with respect to the hole due to junk and materials

(Testimony of Allan A. Anderson.)

that had been left in that particular hole on prior operations. So we decided to plug the well back and set a whipstock at some 130 feet above the old hole and to mill through the casing. We did set a whipstock and milled through the casing and in milling through the casing you have to cut metal from your casing and you must have some means of bringing the cuttings to the surface and so, knowing that, I contacted Mr. Vernon King and explained the situation to him and obtained from him his approval to the use of mud for the purpose of milling through a new window in the casing.

Mr. Dechter: We move to strike out the latter portion of the answer as not responsive, and a conclusion of the witness, and as incompetent for the reason that under the order of this Court such consent had to be in writing, and the statement of the witness he secured his consent is his [368] conclusion.

The Referee: It may be stricken.

Mr. Pallette: Q. Mr. Anderson, at the time that you commenced to mill through the casing on or about the 18th day of May, 1940, did you place a telephone call to Mr. Vernon King, the engineer for the Trustee in Bankruptcy of the Huntington Shore Oil Well?

A. I did. It may be on the 17th of May but anyway I talked to Mr. Vernon King continuously during all operations and consulted and advised

(Testimony of Allan A. Anderson.)

him at all times as to just exactly what we were doing.

Q. At this particular time, however, on the 17th or 18th day of May at the time you commenced your milling operations you had a telephone conversation with Mr. King?

A. I did. That is right.

Q. At that time did you ask him to consent to the use of mud as a circulating medium for the purpose of your milling operations? A. I did.

Q. And did he consent? A. He did.

Mr. Dechter: To which we object as calling for the conclusion of the witness. The question was did he consent, and I move the answer be stricken out for the purpose of the objection.

The Referee: Stricken. Motion to strike is granted that [369] he consented, on the ground of a conclusion.

Mr. Pallette: Q. At the time you made this request of Mr. King during this telephone conversation what did Mr. King say?

A. Why, this was over a period of three or four days the milling operations and cutting this window through the casing, and during that time I was talking with King from once to twice a day with respect to or in regard to the use of mud to drill through our fractured shale bodies from the window down to the top of the oil sand. When we finally milled through the window I asked Vernon

(Testimony of Allan A. Anderson.)

if it would be all right with him if we could continue to use mud to drill through the fractured shale bodies from our window to the top of the oil measure, and Vernon at first said he would have to think it over or talk about it—I think his exact words was to talk about it, so I continued talking with him for the next two or three days and finally obtained from Vernon the right to use mud.

Mr. Dechter: We move to strike out that statement as a conclusion of the witness.

The Referee: It may be stricken.

Mr. Pallette: Q. What did he say?

A. Well, as to the exact wording, we were doing this in personal talks together there in the field and over the telephone, and the exact phraseology of it I can't say. I don't recall that because there were too many conversations. [370] It is an impossibility to remember the exact wording, but Vernon King knew at all times we were using mud and he gave us his consent to use mud.

The Referee: That is a conclusion.

Mr. Dechter: And we move to strike it as a conclusion.

The Referee: It may be stricken. State as near as you can what was said.

A. Well, I am sorry but I cannot quote him word for word. Now, we were talking about the mud—I can tell you this, that in attempting to get Vernon King's O. K. I consulted another party,

(Testimony of Allan A. Anderson.)

which party is interested in the field, and they in turn talked with Vernon King and then after Vern had talked with this party he gave me his consent as to the use of mud.

Mr. Dechter: We move to strike out the statement he gave his consent as to the use of mud as a conclusion of the witness.

The Referee: Motion granted.

Mr. Pallette: Q. Mr. Anderson, cannot you tell us approximately what Mr. King said—not his exact words, but the substance of his statement.

A. I believe his exact words as close as I can come to it it would be, all right to use mud down to the top of the oil sand.

Q. In addition to that, did he not say it was his suggestion you drill forty or fifty feet into the oil sand? [371]

A. Mr. King——

Mr. Dechter: We object to counsel leading the witness.

The Referee: Objection sustained.

A. Mr. King——

Mr. Dechter: Just a moment. There is no question before you.

Mr. Pallette: Will you read back, Mr. Reporter, Mr. Anderson's last answer?

(The reporter read from the record as requested).

(Testimony of Allan A. Anderson.)

Mr. Pallette: Q. Mr. Anderson, did he make any further statement with reference to the drilling of the well at that time?

A. Yes, he did. He recommended that due to his recent experience in the Huntington Beach field that it would be well for us to set our casing some forty or fifty feet into the oil sand.

Q. What did you say to that?

A. I replied to him, "No, Vern. Our agreement with you is when we get to the top of the oil sand that we will use oil and therefore we don't want to jeopardize our position in any manner so we prefer to change over to oil when we get to the top of the oil sand."

Q. Mr. Anderson, you continued to use mud in all your drilling operations from approximately the 17th day of——17th or 18th or 19th, whatever it was, of May up until what time? [372]

A. Up until the time that we had again—I say again because when our casing we pulled it and then had to re-drill our hole until we had gained a depth of 4408 feet which was our correlated marker of where we should encounter the top of the oil sand in the new hole.

Q. What approximately was the date of that?

A. I would say that was in July, the last half of July, the 17th or 18th or 19th.

Q. At that time what did you do?

A. At that time we changed over to oil.

(Testimony of Allan A. Anderson.)

Q. And have you used mud in any drilling operations since that time? A. We have not.

Q. During the period from the time that you just testified that you commenced using mud on or about the 18th of May until the time you changed to oil on or about the 17th day of July, 1940, was Mr. King present at the well at any time?

A. Why, Vernon King was at the well I would say at least every other day, maybe there was periods of three or four-day intervals when he was not present but over that entire period he was in constant contact with the well, either he or Mr. Earl Ross or the Huntington Shore pumpers, and of course I carried on conversations with Vernon King by telephone every few days as well to keep him advised when he didn't happen to be at the well. [373]

Q. When he came to the well or when Mr. Ross came to the well you would discuss with them what you were doing and what circulating medium you were using?

A. Why yes, we discussed the type of mud or, for instance, when we lost circulation we made up a mixture of Aquajel and Fibratex for the purpose of regaining circulation and so forth and Vernon King was there while we were mixing it and it was a matter of a few hours after we lost circulation that we regained it and we were all commenting on the ability of Fibratex to seal off the fractures and so forth.

(Testimony of Allan A. Anderson.)

Q. At no time during this period from the 17th of May to the 17th day of July did Mr. King or any other representative of the Huntington Shore Oil Well ever object to you with reference to the use of mud as a circulating medium in the well?

A. They did not, no. [374]

Redirect Examination

By Mr. Pallette:

Q. I believe you testified, Mr. Anderson, that your correlation shows that you expected to reach the top of the oil sand from which you expected to produce at approximately 4400 feet?

A. That is correct.

Mr. Dechter: To which we object as incompetent and not the best evidence. The correlating he spoke about would be the best evidence.

The Referree: Objection overruled.

Mr. Pallette: Q. When you reached a depth of 4400 feet what did you do?

A. We reached a depth of 4408 feet, Mr. Pallette, and we changed to oil. [410]

Q. No, I am speaking of the——

A. Oh, pardon me. We took a core, yes, at 4400.

Q. And will you explain to the Court what coring is?

A. Coring is the act of obtaining a sample of the formation you are drilling through by the use of a core barrel. A core barrel is very similar to a bit with the exception it has a hole, a hollow space

(Testimony of Allan A. Anderson.)

in the center with a barrel above with a core catcher so that the formation is——you drill around the formation.

The Referee: In other words, it is a means——

A. Of recovering a sample of the formation you are drilling in. It is representative. You receive a sample and pull it to the surface so you can physically make an inspection of the formation you are drilling in.

Mr. Pallette: Q. You had not seen anything in your cuttings which would indicate to you you were already in the sand at the time you stopped actual drilling and commenced coring?

Mr. Dechter: To which we object as leading and suggestive.

The Referee: It is leading. Objection sustained.

Mr. Pallette: Q. Had you seen any sand, any oil sand in your cuttings above the depth of 4400 feet?

A. Why, Mr. Pallette, we had seen sand in our cuttings that we did not identify as the oil sand we wished to produce from. [411]

Q. Excluding the Jones sand?

A. No, we had not. We had been watching the ditch samples and correlating shale.

Q. Why did you core at 4400 feet?

A. We cored at 4400 because our examination and correlations of the various wells I mentioned this morning indicated we should top the oil sand at approximately 4400 feet.

(Testimony of Allan A. Anderson.)

Q. What did your thirteen feet of core show?

A. It consisted of eight feet of shale, some of which was fractured and some of which was solid. Then there was a marker, a white limestone marker varying in width from one inch to three inches. That indicated to us that we were at the top of the oil sand, and then we had approximately four to five feet of oil sand in the lower portion of the core.

Q. That was the first evidence you had that you were in the sand?

A. That is correct, the first evidence we had.

Q. Whereupon, you immediately ceased further drilling? A. That is correct.

Q. Now, referring to——

The Referree: Pardon me. Didn't you say you went down 4408 feet and took your sample and then went down to 4413?

A. Went to 4413? No, we started coring at 4400 feet even but our core was thirteen feet in length. We actually recovered thirteen feet of formation in the core. To 4408 was shale. [412]

Q. But from 4400 feet to 4413 you used mud?

A. Yes. We could not tell exactly where we would pick up the sand. As far as that is concerned, we are under orders of the Division of Oil and Gas, who have police powers over the field, and they stated we should obtain a core of the top of the oil sand before setting casing. We were so advised by the Deputy of the Division of Oil and Gas in writ-

(Testimony of Allan A. Anderson.)

ing so it was necessary to core to comply with their instructions.

Mr. Pallette: Q. Now, referring to the period around the 17th of July, 1940, I believe you testified this morning that you drilled to a depth of some 4800 feet? A. 4858.

Q. At that time you were drilling with oil?

A. That is correct.

Q. And you had been drilling with oil from what depth?

A. We lost our hole as I further testified and then recovered it by directing the hole into the old hole by using the knuckle and whipstock and when we obtained 4408 feet we changed to oil and made the hole from 4408 to 4458 with oil.

Q. Will you explain to the Court what happened when you reached the depth of 4458 feet?

A. Why, the oil—there had been some pressure brought on us by the State to use a lighter-gravity oil than I had been using so we did turn to a lighter-gravity oil and the [413] lighter-gravity oil cut the mud cakes off the wall of the fractured shale body and allowed the shale to come into the hole, lubricated with this light oil, and the fact twenty-three-gravity oil, a column of fluid say 4,000 feet of twenty-three-gravity oil has a lesser weight at the bottom of that column of fluid than is carried in the fractured shale body. Fractured shale body has gas pressure in it of about 1450 to 1500 pounds of pressure so it becomes an absolute impossibility now to

(Testimony of Allan A. Anderson.)

to drill through the lubricated shale body by the use of oil. You can withhold the fractured shale as long as you are applying your pump pressure but when you cease the pressure and pull the drill pipe from the hole then your formation pressure exceeds that that would be created by a column of fluid of twenty-three-gravity oil.

Q. I want you to explain what you physically did. Why didn't you drill any deeper?

A. Why, our pipe started to freeze on us on this fractured shale coming in and it became locked so we pulled our pipe out of the hole.

Q. Then you tried to go back in again?

A. Yes.

Q. How deep were you able to get?

A. Why, I believe the greatest depth we went to was——that is with oil.

Q. Yes.

A. We finally wormed our way and circulated and backed up [414] and one thing another down to 4186 or maybe 4286. I just cannot tell you the exact depth, but between those depths.

Q. It was above 4200 feet?

A. It might have been a little below 4200; might even have been 4210. I couldn't say without the log.

Q. You testified the top of the oil sand was 4408? A. That is correct.

Q. What was the reason you could not go any deeper than approximately 4200 feet?

(Testimony of Allan A. Anderson.)

A. On account of the pressure and the fractured shale being lubricated with oil, permitting the shale to come in and freeze the pipe. When shale runs in it draws friction on your drill pipe over a long space like two or three hundred feet, and the final section we pulled out, the casing had caved into the hole and pulled it up a couple of hundred feet.

Q. And your hole is full of shale? A. Yes.

Q. And that is why you could not go down further without re-drilling?

A. That is right, due to gas pressure. This gas pressure also aerates your light-gravity oil which again lightens the ability of your oil to apply pressure to the shale body.

Q. When you stopped drilling your hole was only open to approximately 4200 feet, is that correct?

A. I would say that is right, yes. [415]

Q. So far as you know, that is the condition of the hole at the time the well was transferred to the McCallen Corporation? A. Yes sir [416]

[Endorsed]: Filed October 10, 1940. Ernest R. Utley, Referee.

[Endorsed]: Filed December 31, 1940. R. S. Zimmerman, Clerk. [416]

[Title of District Court and Cause.]

REPORTER'S TRANSCRIPT
OF

1. Further hearing on return of order of February 9, 1941, to George T. Goggin, to show cause any the certificate of contempt filed December 31, 1941, should not be dismissed.

2. Hearing on return of order of January 13, 1941, to Bolsa Chica Oil Corporation, Thomas W. Simmons, Allan A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation and W. H. Cree to show cause why they should not be adjudged in contempt pursuant to the certificate of the referee.

APPEARANCES:

Mr. Raphael Dechter, and
Mr. J. J. Rifkind.
For Trustee.

Overton, Lyman & Plumb,
By Mr. Eugene Overton and
Mr. W. S. Pallette.
For Bolsa Chica Oil Corp.,
Thomas W. Simmons and
Allan A. Anderson.

Mrs. Elizabeth Hensel,
For H. H. McVicar, C. M. Rood,
M. M. McCallen Corp. and W. H. Cree.

Mr. W. H. Cree, in pro. per. [417]

Los Angeles, California,
Thursday, January 30, 1941, 10 A. M.

The Court: A calendar matter?

The Clerk: Yes. In the Matter of Jack Dave Sterling, Bankrupt.

1. Further hearing on return of order of February 9, 1941, to George T. Goggin, Trustee, to show cause why the certificate of contempt filed December 31, 1941, should not be dismissed.

2. Hearing on return of order of January 13, 1941, to Bolsa Chica Oil Corporation, Thomas W. Simmons, Allan A. Anderson, H. H. McVicar, C. M. Rood, M. M. McCallen Corporation and W. H. Cree to show cause why they should not be adjudged in contempt pursuant to the certificate of the referee.

The Court: Proceed, gentlemen.

Mr. Dechter: Your Honor will recall that at the conclusion of the hearing the other day your Honor said he would consider the matter of the objection to the jurisdiction, and if the court desired any further argument by counsel you would so advise us. Now, I have some additional cases, if the court desires to have them.

The Court: I think I had better state my thought at the present time. I will hear further argument. Perhaps further argument may clarify my own thought, because I have not reached definite conclusions in the matter, so I sent [456] for the peti-

tion. I think the certificate of the referee should contain not merely the order, but the petition on which the order was made, because the violation which is charged is contempt. The certificate is like a selective judgment roll. In any judgment roll the petition or the complaint upon which the order was made is a necessary part of the record. So I sent for them. The question arose on a petition for instructions; is that correct?

Mr. Pallette: That is correct.

The Court: The petition was filed on April 20, 1940, and on that petition the order to show cause was directed to Bolsa Chica Oil Corporation, and the hearing was had, as a result of which the order of May 5th was entered, which order has become final through the failure to petition for review by this court. [457]

The Court: Gentlemen, I have given a little further thought to this matter. In fact, I spent the entire noon hour in my chambers in going over the record in the case in the hope that there was some additional light I could find on the subject. And my conclusion is that we are dealing here not with a proposition where the bankruptcy court, not having the right to determine certain matters by summary proceedings, proceeds to determine them nevertheless, thus bringing into question the proposition whether the objector is bound by the record, the finality of which he did not see fit to challenge. I think the difficulty confronting us here arises from the fact that a situation like this does not seem to

have arisen in any of the cases which the industry of counsel and my own industry have [505] been able to discover.

I think it cannot be denied that in matters which come under Section 23 of the Bankruptcy Act, in controversies between a trustee and adverse claimants to property acquired or claimed by the trustee, the exception in subdivision (b) of that section applies. That is, where the trustee asserts a right to property the adversary, if he have possession of the property, need not submit to summary determination turn-over proceedings, but insist on a plenary action being brought, but if he does insist he may, by participating in a proceeding, perhaps waive his right to challenge jurisdiction, or by failing to properly raise the question may waive it, or by doing other acts which are tantamount to such a waiver.

Perhaps the case in which the strongest language is found to support the position of the trustee is In re Murray. I realize that much of the language that is used there is merely by way of theorizing, because ultimately the court disposes of the actual controversy in the very paragraph in which he states that Murray had not protected his rights; had practically waived them. I like pretty writing myself. I like to theorize. We are safer to do it in an article than to do it in an opinion. The court there, after giving the quotation from the McDonald case, says this:

"Here, appellant filed his answer to the show [506] cause order upon the merits. He volun-

> tarily conveyed the property to the trustee in bankruptcy to abide the outcome of the hearing; he presented all of his evidence upon an accounting. It was too late for him thereafter for the first time to question the jurisdiction of the court over the subject matter. He had waived his personal privilege of demanding that the cause of action be asserted in a plenary proceeding. He must be held to have consented to the jurisdiction."

So that even in those particular cases where the objection is not, to use the phrase from the municipal law, to the existence of the power but to the mode of its exercise there must be some strong affirmative action before consent to jurisdiction is presumed. And that is in line with the general proposition that there is no presumption in favor of jurisdiction in the federal courts, because they are courts of limited jurisdiction, made so by the Act of Congress of the United States, which began with 1789, and in subsequent legislative action they have simply declined to give to the federal courts the full constitutional jurisdiction, but have hamstrung our jurisdiction by diversity of citizenship and by requirements that the controversy be in excess of the value of $3,000. [507]

This morning I gave some of the illustrations where the Supreme Court, in dealing with its own powerful jurisdiction, has declined to entertain actions in advance of actual controversy or harm ac-

tually done. Those cases, of course, include the declaratory judgment statute, but if we examine the famous case of Ashwander v. Valley Authority, 297 U. S. 288, we find that in that opinion the court reasserts that principle in each one of the cases I have cited. The court says, at page 324:

> "The judicial power does not extend to the determination of abstract questions. * * * It was for this reason that the court dismissed the bill of the State of New Jersey which sought to obtain a judicial declaration that in certain features the Federal Water Power Act exceeded the authority of the Congress and encroached upon that of the State. New Jersey v. Sargent, 269 U. S. 328. For the same reason, the State of New York, in her suit against the State of Illinois, failed in her effort to obtain a decision of abstract questions as to the possible effect of the diversion of water from Lake Michigan upon hypothetical water power developments in the indefinite future. New York v. Illinois, 274 U. S. 488. At the last term the Court held, in dismissing the bill of the United States against the State of West Virginia, that general [508] allegations that the State challenged the claim of the United States that the rivers in question were navigable, and asserted a right superior to that of the United States to license their use for power production, raised an issue 'too vague and ill-defined to admit of judicial determination.' United

States v. West Virginia, 295 U. S. 463, 474. Claims based merely upon 'assumed potential invasions' of rights are not enough to warrant judicial intervention. Arizona v. California, 283 U. S. 423, 462.

"The Act of June 14, 1934, providing for declaratory judgments, does not attempt to change the essential requisites for the exercise of judicial power. By its terms it applies to 'cases of actual controversy', a phrase which must be taken to connote a controversy of a justiciable nature, thus excluding an advisory decree upon a hypothetical state of facts."

I think it is well to review for the record how these proceedings were instituted. The defendants —we will call them defendants in this contempt proceeding—were not brought into court upon an allegation that a controversy existed between them and the trustee in regard to anything. That upon the affidavit of a geologist and upon the affidavit of the bankrupt and the verified petition, an order to show cause was issued. The verified petition merely stated: [509]

"That petitioner is informed and believes and on that ground alleges that the proposed course of redrilling said 'Petroleum Well' will cause the same to come within 100 feet of the 'Huntington Shore Well' of the above entitled bankrupt estate, which is situated on that certain real property in the County of Orange,

State of California, more particularly described as follows: * * * covered by Easement No. 309-21 granted by the State of California.

"That petitioner is further informed and believes and on that ground alleges that the surveys, as plotted, and their intersection with the inclined planes show that it will be impossible to redrill the 'Petroleum Well' without coming within 100 feet of the oil sands perforated by and from which production is obtained by the 'Huntington Shore Well', particularly at 3700 feet, 3800 feet, 3900 feet, and 4000 feet, and thereby causing infiltration of oil, mud, cement and other foreign substances, and that the same will result in irreparable damage to and possible loss of said 'Huntington Shore Well'."

Then was given the date that the Huntington Shore Well was placed on production and reference was made to the affidavits.

"Wherefore, your petitioner, by reason of the value of said well and the irreparable loss and [510] damage which will possibly result thereto by reason of the redrilling of the said 'Petroleum Well', desires that the court give instructions to said petitioner as to the action and proceedings which should be taken by the Trustee in Bankruptcy in the matter."

The order to show cause merely stated that the Bolsa Chica Oil Corporation is ordered to appear

before the Referee in Bankruptcy and "show cause, if any it has, why such order or orders should not be made and entered by the above entitled court in the above entitled matter to protect the 'Huntington Shore Well' of the above entitled bankrupt estate from damage resulting from the redrilling of the 'Petroleum Well', and why such additional further and future order or orders should not be made and entered authorizing the Trustee in Bankruptcy to institute, maintain and prosecute any action, proceedings or suit in this or any other court which may, in the opinion of the Trustee in Bankruptcy, be necessary or advisable to protect the 'Huntington Shore Well' from damage as the result of the redrilling of the 'Petroleum Well' ".

There is no allegation of any controversy or any demand having been made; merely that somebody examined the survey and is satisfied that it is likely to cause this damage as, if and when they drill in accordance with the plan. Neither the order to show cause intimated nor did the [511] petition intimate that an injunction would be asked to enjoin them from proceeding in the manner intended. The hearing was had. From the very beginning we find objection to the jurisdiction of the court to hear and determine the matter. I have read the beginning and the end of the transcript. And, in fact, sometimes when you have language read to you it sounds differently, so I sat on the couch and had Mr. Somers read to me the colloquy of counsel so that I could reproduce, as it were, what took place

before the Referee. And while there is some intimation at the end that some order might be agreed to, throughout the entire proceedings the Bolsa Chica Oil Corporation, respondent, protested the jurisdiction of the court to hear the matter, both upon the proposition that they were not before the court and upon the proposition that they are not trespassing anybody's property, that they intend to drill on their own property, and that the Referee in Bankruptcy had no right whatsoever to tell them, in advance of a commission of any tort, not to act with their property in a certain manner.

We are not dealing here with an adverse claim for property as between a trustee in bankruptcy and a stranger. That phase of the case is entirely eliminated. That is why all the teachings of these cases dealing with controversies relating to property and the waiver of any right thereto by consenting or not objecting to summary proceed- [512] ings, as set forth in patent law, do not help us at all. Here we are dealing with the right of a court of bankruptcy to hale before it, and on an order to show cause, a person who owns adjoining property and saying to him, "My trustee is asking for instructions." And when he comes into court he is confronted with the proposition, not upon the basis of what he is doing, but upon the basis of what happened to somebody else when somebody else tried to drill in the proximity of the land, and upon that basis he finds himself subject to an interdict,

by a court whose jurisdiction he has challenged throughout, not to deal with his own property in the manner in which he chooses on pain of contempt.

When we are dealing with that kind of property we are dealing with a mere fundamental right, and that is the right guaranteed by law to a person, subject to governmental regulation, of course, to use his property as he sees fit, being responsible for any damage when he does it.

There is no relation between the Bolsa Chica Oil Corporation and the bankrupt estate. They were not bound by any contract. It is true that they leased from the same State of California, but they did not have a pool agreement or any of those contracts which might give them reciprocal rights. They are just strangers dealing with their own property as they saw fit, subject to the rule not to damage another. [513]

Right from the beginning, and this is from page 2 of the transcript, we find this:

> "Mr. Borden: At this time I would like to say we are here in obedience to the order to show cause. I am representing the Bolsa Chica Oil Corporation. While, of course, we concede your Honor's authority to make any orders you may deem necessary with respect to directing the Trustee in his work, we do not concede any jurisdiction to make any order that would affect us in this proceeding, we not being a party

to the proceeding, but are appearing only specially here and are not submitting to the jurisdiction of the court.

"The Referee: You are objecting to the jurisdiction of the court to make any orders affecting your company?

"Mr. Borden: Yes, your Honor.

"Mr. Dechter: May it please the court, even if that objection was well-founded this court must necessarily receive evidence to be able to rule on that objection. In other words, it must receive sufficient evidence to determine whether or not the court has summary jurisdiction.

"The Referee: Yes, I think that is true."

Then Mr. Dechter asserts the power of the court, by summary order, to bind Bolsa Chica Oil Corporation. Then he used the analogy of a trustee operating a department store.

"The Referee: * * * I don't think this court would [514] have any jurisdiction to prevent this company or any other company from drilling a well, but if it interfered or threatened to interfere with the bankrupt's property in any way, I think to that extent the court would have jurisdiction.

"Mr. Borden: Under the very allegations of the petition, your Honor, it does not appear we are in any way trespassing upon the property of the bankrupt. In other words, we are

drilling from our own drill-site. We are not trespassing on their property according to the very allegations of the petition. I am not here to offer any objection or demurrer because we are appearing here objecting to the jurisdiction of the court.

"The Referee: Your objection may appear; however, the court must examine in a preliminary way this matter in order to determine whether or not it does have the jurisdiction.

"Mr. Borden: I appreciate that, your Honor.

"The Referee: Very well, you may proceed."

I have gone into this rather fully, gentlemen, because it is a phase on which I have not expressed myself very fully and, also because, I am frank to say, I was strongly impressed at first with the thought that perhaps there was a consent decree here. But the more I study the decree the more I am convinced that that is not the case. I will go into that matter in a moment.

I want to show from the record, which is also before us [515] as a part of this, that there was not at any time any information that jurisdiction was being conceded and it was challenged at all times. When the cross examination began, I think the very first cross-examination, Mr. Borden made it very clear that by cross-examining the witness he was not waiving his objection to the jurisdiction.

I have lost the place where it occurred, but I find it again at the end, and the Referee confirmed the statement of Mr. Borden. On page 82 we find this:

"The Referee: Any further testimony?

"Mr. Dechter: That is all for the petitioner, for the Trustee.

"Mr. Borden: I think I made the statement in the first instance that our cross-examination was not to be construed as any waiver of our objection to the jurisdiction.

"The Referee: Oh, yes.

"Mr. Borden: I don't think there is any question about that. We have no evidence to offer at the present time. I might have if there is any question in your Honor's mind whether or not the court, in a summary proceeding of this kind against a total stranger, and under these circumstances, has a right to take any action or to restrain us from proceeding. I should like to have a continuance in order to put on some testimony without conceding the jurisdiction of the court. I think the court is entitled to have the benefit, no matter what order it makes with respect to [516] directing the Trustee to commence plenary action or any other remedy available to him, of hearing testimony on both sides."

Later on, when the question of the form of stipulation came up, on May 1st, we find this:

"The Referee: Have you accomplished anything in the matter of Jack Dave Sterling?

"Mr. Rifkind: Yes, your Honor. We have reached a stipulation that an injunction may be issued by the court against the Bolsa Chica Oil Corporation. We have already given the specific language to the reporter and I would like him at this time to read it to the court.

"The Referee: Is the stipulation generally agreed to between counsel?

"Mr. Borden: Yes.

"The Referee: You may state generally what it is.

"Mr. Borden: We have stipulated as to the order. We do not concede jurisdiction of the court. We are going to agree that we will not review the order of court and will be bound by the order. However, I make that statement because we do not want to generally concede jurisdiction."

Then follows the statement of the Referee that as far as he is concerned you could review the order. Then the wording of the stipulation is read and nothing more seems to appear except general questions relating to the order [517] to be prepared.

Mr. Dechter: There is a further statement by Mr. Borden that the stipulation is agreeable.

The Court: Yes, that is right. This is what it says:

"Mr. Rifkind: All right.

"The Referee: Is that stipulation agreeable, gentlemen?

"Mr. Borden: Yes.

"Mr. Rifkind: We will prepare an order.

"The Referee: Very well, prepare a formal order.

"Mr. Rifkind: It will be approved as to form and contents by both sides."

Now, we get to the order itself and we find that unless we eliminate some phrases reserving jurisdiction it shows clearly on its face that jurisdiction was reserved. The only jurisdiction that was before the court is the jurisdiction to hear the matter and bind them by any kind of an order. That is what they are talking about. The order, of course, like all composite orders which are the result of compromise between counsel, is not a model. And, in my opinion, that is due to the fact that it was drawn by one side, and then additions were made. There are phrases here which could have been reworded and one or two which could have been eliminated and left the matter clearer than it is. In the first place, there is a recital here right from the very beginning, page 1, line 21:

"The Bolsa Chica Oil Corporation, upon the calling [518] of the matter, announced that it was appearing specially for the sole purpose of objecting to the jurisdiction of the court to make any order affecting said corporation;"

That is a challenge to the entire jurisdiction.

> "that thereupon the court informed counsel that it would withhold ruling upon the question of jurisdiction until sufficient evidence was introduced to determine the question: That oral and documentary evidence was introduced upon the part of the Trustee in Bankruptcy and the witnesses called on behalf of the Trustee in Bankruptcy were cross-examined by the attorneys for the Bolsa Chica Oil Corporation; the Bolsa Chica Oil Corporation, having at the conclusion of the introduction of oral and documentary evidence upon behalf of the Trustee in Bankruptcy, stipulated in open court to the granting of the injunction as hereinafter more particularly set forth, the Bolsa Chica Oil Corporation stating that such stipulation was subject to the objection of the jurisdiction of the court".

That is the objection heretofore made. They use the word "jurisdiction"; not the word "general". Then, this is a phrase that could very well have been omitted, but it certainly does not detract from the preceding one: "and that such stipulation was not intended to confer general jurisdiction on the court." The use [519] of the word "general" there is not an absolute one, but it merely states negatively what is already stated positively, that the stipulation merely related to the form of the order

to be made. The defendant insisted then, as he had before, that they did not concede jurisdiction.

Incidentally, there is another paragraph here, before the adjournment on the last date. Mr. Borden made this statement, which appears on page 85, after the discussion as to distance:

> "Mr. Pallette: I wouldn't be surprised but what we could stipulate to one hundred feet, but I don't think I am justified in doing so without consulting our engineers.
>
> "Mr. Borden: I think that is a good idea. Let the record show, if your Honor please, that by suggesting that we are willing to submit to the jurisdiction of the court, that we do not do so until we actually do so."

In other words, he just says, "Perhaps I will agree to it or not object to it, but I am still not ready to do it and may insist upon my point of jurisdiction."

Referring back to the order:

> "The court having been fully advised in the premises and the court having overruled the objection of the Bolsa Chica Oil Corporation to the jurisdiction of the court, it is, therefore, ordered as follows:

Now, there is a notation here, "Approved as to form and contents." The form does not comply with our rule. [520] The form provided by the rule is merely, "Approved as to form." And *is* counsel

desire to waive objection to the matters other than form then they have to write in the direct words, "No objection to the entry of the order," or words of similar import. So I do not think that adds anything to it, because I am satisfied of the reservation, in a rather round-about manner, of jurisdiction. It is absolutely apparent and I do not think anybody was deceived by it.

There is one other proposition we must bear in mind. Counsel have stated repeatedly that this is a collateral attack. This is not a collateral attack. This is a direct attack. A citation for contempt is a direct proceeding arising ancillary to another, and when you attack an invalid order in a contempt proceeding you are attacking it directly; not collaterally. In other words, a man need not submit to an order or go to the trouble of an appeal from an order of court which he challenges is without jurisdiction. If the order is void because of lack of jurisdiction he can attack it any time. Orders are repeatedly made that way. What is that habeas corpus case?

Mr. Pallette: Rowland?

The Court: I have even a more constructive case, gentlemen, and one that to my mind, unless our ideas of [521] courts change more rapidly than even I would like to see them change, is still good law. It is fundamental that you are not bound to obey an order that is invalid. You may disobey it and then, in a proceeding based on it, you may at-

tack its validity, for this reason: The person who cites you for contempt brings the order into court. It is the basis of the order and you are not attacking it collaterally when you say, "This is not a valid order." You are challenging the foundation for the citation, a foundation which they must establish exists. Therefore, an attack, either by habeas corpus after conviction or in any other manner in a contempt proceeding, of the order made in the main proceedings is a direct attack. Ex Parte Sawyer is, to my mind, the most interesting that I have been able to find on that point. I went at it backwards. I started with about 280 and examined about 7 or 8 cases, working backwards. I found it as the leading case on the subject and the best case under the law. Ex Parte Sawyer, 124 U. S. 200 decided in 1888 and cited repeatedly since, is one of the cases cited by Mr. Justice Holmes in one of the late cases on the subject. And I am quite sure that such a liberal as Mr. Justice Holmes would not have approved the doctrine if he felt it did not correctly express his views of civil rights. In this case the City Council of Lincoln, Nebraska, was about to remove from office a police judge upon the ground that he had illegally kept some fees. [522] So the police judge, Albert F. Parsons, went before the federal District Court on the circuit side —that was at a time when our courts were divided into district courts and circuit courts, personified in the same judge; the one court heard law and

jurisdiction cases and the other heard equity cases—and alleged the fact that the City Council was about to meet for the purpose of removing him from office. Upon the basis of that sworn petition and affidavit he secured an injunction enjoining the mayor and City Council from holding the meeting. They disobeyed the order, and held the meeting, and removed the police judge. So the police judge went before the court and satisfied the court that his dignity had been outraged and flaunted and that they had robbed him of a lawsuit which he had alleged was within the jurisdiction of the federal court, because he was being deprived of rights under the constitution, the due process and constitutional laws of the United States. An order to show cause was sent to the mayor and council and the judge promptly found them all guilty of contempt of court and fined them in sums ranging from $50 to $600 which, of course, at that time was a lot of money, or stand committed to the custody of the marshal until the fines were paid. They declined to pay and were committed to the marshal. Whereupon a writ of habeas corpus was sued out on behalf of the contenders, and in the petition for writ of habeas corpus it [523] was alleged:

> " 'That the court had no jurisdiction of said suit commenced by said Albert F. Parsons against your petitioners, and that said restraining order was not a lawful order, and that said judgment of said court that your petitioners

were in contempt, and the sentence of said court, that your petitioners pay a fine and suffer imprisonment for violating said restraining order is void and wholly without the jurisdiction of the Circuit Court of the United States, and in violation of the Constitution of the United States'; and further alleged 'as special circumstances, making direct action and intervention of this court necessary and expedient, that it would be useless to apply to the Circuit Court of the United States for the District of Nebraska for a writ of habeas corpus, because both the circuit and district judges gave it as their opinion in the contempt proceedings that the said restraining order was a lawful order and within the power of the court to make.' "

So they appealed, in the language of the famous bishop, from the guardians of the God's truth direct to the God himself. They appealed to the highest court.

Mr. Dechter: The mayor and the councilmen had never appeared in the injunction proceeding and it was an ex parte injunction against them. [524]

The Court: But they were served with the process.

Mr. Dechter: That is what the Supreme Court points out in this case of Chicot County Drainage District.

The Court: Well, I will let you make new law on this case. I want to see if you can send a man to

jail or penalize him thousands of dollars because of his failure to appeal. You can't show me any law and you haven't so far shown me any law to the effect that if a man challenges the jurisdiction of a court his only recourse is appeal.

Mr. Dechter: That is what the three Supreme Court decisions hold.

The Court: They don't say that as I read them. You read them differently than I do.

Mr. Dechter: The jurisdiction over the subject matter was challenged.

The Court: I don't reconcile this with the other. I think this is a contempt proceeding of much greater weight. It is based on the constitutional ground that nobody is required to obey an order of a court that is without jurisdiction of the subject matter.

Here was a federal court. Its jurisdiction was invoked in a State matter. This is exactly what the court said. In discussing the problem of whether there was jurisdiction, civil or criminal in nature, Mr. Justice Gray said:

> "But if those proceedings are to be considered as neither criminal nor judicial, but rather in the [525] nature of an official inquiry by a municipal board intrusted by the law with the administration and regulation of the affairs of the city, still, their only object being the removal of a public officer from his office, they are equally beyond the jurisdiction and control of a court of equity.

"The reasons which preclude a court of equity from interfering with the appointment or removal of public officers of the government from which the court derives its authority apply with increased force when the court is a court of the United States and the officers in question are officers of a State." I am omitting.

"In any aspect of the case, therefore, the Circuit Court of the United States was without jurisdiction or authority to entertain the bill in equity for an injunction.

"As this court has often said: 'Where a court has jurisdiction, it has a right to decide every question which occurs in the cause; and whether its decision be correct or otherwise its judgment until reversed, is regarded as binding in every other court. But if it act without authority, its judgments and orders are regarded as nullities. They are not voidable, but simply void.' Citing cases. [526]

"We do not rest our conclusion in this case, in any degree, upon the ground suggested in argument; that the bill does not show a matter in controversy of sufficient pecuniary value to support the jurisdiction of the circuit court; because an apparent defect of its jurisdiction in this respect, as in that of citizenship of parties, depending upon an inquiry into facts which might or might not support the jurisdiction, can be availed only by appeal or writ of

error, and does not render its judgment or decree a nullity."

Citing cases.

"Neither do we say that in a case belonging to a class or subject which is within the jurisdiction both of courts of equity and of courts of law, a mistake of a court of equity, in deciding that in the particular matter before it there could be no full, adequate and complete remedy at law, will render its decree absolutely void.

"But the ground of our conclusion is that whether the proceedings of the City Council of Lincoln for the removal of the police judge, upon charges of misappropriating moneys belonging to the city, are to be regarded as in their nature criminal or civil, judicial or merely administrative, they relate to a subject which the Circuit Court of the United States, [527] sitting in equity, has no jurisdiction or power over, and can neither try and determine for itself, nor restrain by injunction the tribunals and officers of the State and city from trying and determining.

"The case cannot be distinguished in principle from that of a judgment of the Common Bench in England in a criminal prosecution, which was coram non judice; or the case of a sentence passed by the Circuit Court of the United States upon a charge of an infamous

crime, without a presentment or indictment by a grand jury."

Citing cases.

"The circuit court being without jurisdiction to entertain the bill in equity for an injunction, all its proceedings in the exercise of the jurisdiction which it assumed are null and void. The restraining order, in the nature of an injunction, it had no power to make. The adjudication that the defendants were guilty of a contempt in disregarding that order is equally void; their detention by the marshal under that adjudication is without authority of law, and they are entitled to be discharged."

It is interesting to read a concurring opinion of Mr. Justice Field:

"I concur in the judgment of the court, that the Circuit Court of the United States had no jurisdiction [528] to interfere with the proceedings of the Mayor and Common Council of Lincoln for the removal of the police judge of that city. The appointment and removal of officers of a municipality of a State are not subjects within the cognizance of the courts of the United States. The proceedings detailed in the record in the present case were of such an irregular and unseemly character, and so well calculated to deprive the officer named of a fair hearing, as to cause strong comment. But, however irregular and violent, the remedy

> could only be found under the laws of the State and in her tribunals. The police judge did not hold his office under the United States, and in his removal the Common Council of Lincoln violated no law of the United States." * * *

I cannot see any distinction between the situation we have here, except a different charge of illegality, and the situation we have here. The record here clearly shows that what the bankruptcy court proceeded to do was to declare in advance of the commission of a tort, that a tort was about to be committed, and enjoined its commission. I doubt very much that even under the declaratory judgment statute such a declaration could be enforced. The other day I referred to an English case upon the subject, the case of Thomas vs. Moore, 1 Kings Bench 555. In that case a conspiracy had been alleged. [529] No damages as a result of the conspiracy were assessed. The trial judge, however, granted a declaration. The court, in dismissing the judgment and entering one for the defendants used this language:

> "It may be convenient to have a claim for a declaration as to the rights of the parties in respect of contracts extending over a long space of time, and not to wait until there is a breach to have the rights determined. But I have never heard of a declaration that a defendant is doing wrong, unless perhaps it is followed by a statement that damage has accrued or is likely

> to accrue, and that the defendant threatens to continue his wrongful act against the plaintiff. The claim was for damages for conspiracy, and no damage was proved. The two judgments cannot stand together, and judgment must be entered for all the defendants on the claim or conspiracy." [530]

Under the law of California it is a complete defense to an action if it is prematurely brought. In fact, we have a section of the code that deals with it, and the Supreme Court, in interpreting it, has held repeatedly that it is a complete defense.

I call attention to the Ashwander case. And I will call your attention to a recent opinion of my own, Redlands Foothill Groves v. Jacobs, 30 Fed. Supp., 995, in which, in declining to interfere with the enforcement of the Wage and Hour Act, in so far as it applies to agriculture, I used this language:

> "Courts have refused to give relief under it when there was not an actual threat of injury, but merely a fear or apprehension of damages."

Mr. Dechter: I don't want to appear impertinent, may it please the court, but in this Stoll v. Gottlieb case, Ex Parte Sawyer was cited by the losing side and disregarded by Justice Reed and the rest of the court.

The Court: Well, they did not distinguish it. It is very seldom that I am bothered with questions of jurisdiction as I have been bothered in this case, and the reason why it is so important in this case

is quite apparent from its very nature. This order, in addition to enjoining the defendants, also gave authority to the trustee to institute action for damages or for injunctive relief. They were brought here on a contempt citation [531] and it was insisted that the court penalize them for the violation of this injunction of the court. In other words, the court has power to impose a fine and impose it by way of damages, then allow the estate later on to assess additional damages for the loss caused by the acts themselves after the court had imposed the penalty for violation of its interdict. The courts lately have scrutinized records and have raised questions relating to jurisdiction when the thought never occurred to counsel and was never even suggested by counsel to the court below. I feel, in a case of this character, where the challenge over jurisdiction has been made, the court should inquire into it. I am satisfied that the court has no jurisdiction whatsoever and that their appearance and response to an order to show cause, which they have to obey under penalty of having default taken against them, didn't constitute a waiver. And if, as I believe, it is beyond the power of the bankruptcy court to, in effect, make a declaration that unless the well is drilled in a certain way damage will result and the man will be enjoined from doing something on his own property, property which is not the subject of bankruptcy, his actions therein, in the failure to review, does not involve a waiver on his part.

I take it as an uncontroverted proposition that an invalid order, issued against a person in a proceeding to which he may have been an adversary and to which he objected, [532] can be attacked in two ways: That is, one, by appealing and, two, by not appealing and challenging it as being void and showing it is void. And that such an act is not a collateral attack but a direct attack because, after all, when you actually base a citation upon an order you bring up the order yourself, and any showing of invalidity which appears on the face of the record is available in the matter.

Rather than send these back to the Referee I shall order the clerk to make the petition and the order a part of the record in this proceeding. They should have been included in the certificate of the Referee so that there would be a showing of the basis upon which the order was made. These constitute the pleadings upon which the order was made.

Mr. Dechter: Exception noted by the trustee. As I understand it, in order to make the record clear, the court sustains the objection to the jurisdiction?

The Court: Yes.

Mr. Dechter: And refuses to hear the matters raised on the order to show cause in regard to the contempt, by reason of its sustaining the objection to the jurisdiction.

The Court: Yes. You can go to the court and get a mandamus.

Mr. Dechter: I also want to make clear that by its [533] order the court is vacating the injunction heretofore made. I don't believe that is involved in this proceeding, except indirectly.

The Court: I am making a finding that it is void on its face.

Mr. Dechter: Then I would like to ask this court to exercise its power as a Chancellor in Equity to stay the effect of its order stating that it is an invalid order pending an appeal, so that our rights are protected in the meantime. On behalf of the Trustee I would ask that that, at least, be given. We will be diligent in prosecuting the necessary steps on appeal.

The Court: There should be a formal order here upon this hearing. I do not know whether a formal objection——

Mr. Dechter: A verbal objection was made here. There was no written objection.

The Court: I know there was no written objection.

Mr. Dechter: I am willing to have counsel prepare the order and submit it to me, or I will be glad to prepare it and submit it to him, whichever the court desires.

Mr. Pallette: I think we should prepare it.

Mr. Dechter: May it be submitted to me before it is signed?

The Court: Yes. I think it is no more than right that in a matter of this character you——

Mr. Dechter: In other words, this is the most valuable [534] asset of the estate. If this is lost it means about $400,000.

The Court: I will call your attention to this about mandamus: The Circuit Court has recently used some very strong language in regard to a case that arose in my department where I dismissed a complaint and, rather than appeal, they sought to mandamus me to restore it and hear the matter on its merits. However, this is a little different matter.

Mr. Dechter: I will be glad to do both, your Honor. In other words, I have no desire to——

The Court: It might have been the line of least resistance for me to have heard the evidence. It wouldn't have given me nearly the trouble. I have worked very hard on it and I am very thoroughly convinced that it would be a broad extension of the powers of the bankruptcy court if we were to determine that it could issue injunctions of this character.

(Discussion off the record.)

The Court: It is rather a departure from the rules to require a bond of a trustee. I can see where a matter of this kind may result in a good deal of damage to the parties, but I will give the matter further thought, gentlemen, at the time you present the order. Leave the question of the bond open, leave a blank there, or draw an order in the alternative, one with bond and one without bond. [535]

Mr. Rifkind: That order is to be presented to counsel before being signed by your Honor?

The Court: Oh, yes.

[Endorsed]: Filed March 13, 1941. R. S. Zimmerman, Clerk. [536]

[Endorsed]: No. 9790. United States Circuit Court of Appeals for the Ninth Circuit. George T. Goggin, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt, Appellant, vs. Bolsa Chica Oil Corporation, a corporation, Thos. W. Simmons, Allan A. Anderson, William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation, a corporation, Appellees. Transcript of Record. Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

Filed April 14, 1941.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 9790

In the Matter of

JACK DAVE STERLING,

Bankrupt.

STATEMENT OF POINTS UPON WHICH APPELLANT WILL RELY IN THIS APPEAL

1. The District Court erred in rendering the order dismissing the Referee in Bankruptcy's Certificate of Contempt.

2. The District Court erred in sustaining objections to the jurisdiction of the District Court to hear the matter arising under the Referee's Certificate of Contempt.

3. The District Court erred in permitting a collateral attack to be made upon the jurisdiction of the Referee to render the injunction, (the violation of which was the basis of the Referee's Certificate of Contempt), said injunction having become final, and no appeal or other manner of review permitted by law having been taken therefrom.

4. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt) for the reason that the bankruptcy court is a court of equity and as such has inherent power to enjoin threatened harm to,

or interference with, the property in custody of the bankruptcy court.

5. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt) for the reason that the bankruptcy court is given power, under Section 2(15) of the Bankruptcy Act of 1938 to enjoin any threatened harm to, or interference with, the property in custody of the bankruptcy court.

6. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt), for the reason that respondents are estopped from asserting such objections by virtue of their having submitted themselves to the jurisdiction of the bankruptcy court by stipulating that the injunction might be entered against them, by cross-examining the witnesses and otherwise participating in the proceedings against them.

7. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt) for the reason that respondents are estopped from asserting such objections by virtue of their having failed to take an appeal or review from the injunctive proceedings before the Referee.

8. The District Court erred in failing to hold that any purported reservation of jurisdictional ob-

jections by the respondents was waived and nullified by the effect of the general appearance made by respondents in stipulating that the injunction might be entered against them and by approving the order of injunction not only as to form but as to contents as well.

9. The District Court erred in not considering the Certificate of the Referee and not hearing any evidence offered in addition thereto, because said evidence would have shown that respondents interfered with the property in the custody of the bankruptcy court and did so wilfully and intentionally, and with full knowledge of the harm being done the property in custody of the bankruptcy court; and that such conduct constitutes contempt of court even had there been no injunction.

Dated this 11th day of April, 1941.

RAPHAEL DECHTER &
JOSEPH J. RIFKIND
By R. DECHTER
Attorneys for Appellant

Receipt of copy of the within instrument is acknowledged this 11th day of Apr., 1941.

OVERTON, LYMAN & PLUMB
By E. RINGE

[Endorsed]: Filed Apr. 14, 1941. Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

DESIGNATION OF CONTENTS OF RECORD ON APPEAL

Appellant herein designates the following portions of this record, proceedings and documents to be contained in the record on appeal:

1. Debtor's Petition under Section 74 of the Bankruptcy Act, filed on October 14, 1935.

2. Order approving Debtor's petition under Section 74 of the Bankruptcy Act, filed on October 14, 1935.

3. Petition by debtor for adjudication, filed November 23, 1935.

4. Adjudication and order of reference filed November 26, 1935.

5. Reference to the Honorable Ernest R. Utley, filed April 1, 1936.

6. Order Appointing Hubert F. Laugharn as Trustee in Bankruptcy filed January 6, 1936.

7. Order appointing George T. Goggin as Trustee in Bankruptcy, filed January 7, 1941.

8. Petition of Trustee for instructions relative to Huntington Shore Well, filed April 20, 1940.

9. Order to show cause on Bolsa Chica Oil Corporation, filed April 20, 1940.

10. Affidavit of Vernon L. King in connection with the petition for instructions relative to Huntington Shore Well, filed April 20, 1940.

11. Affidavit of Jack Dave Sterling in connection with petition for instructions relative to Huntington Shore Well, filed April 20, 1940.

12. Exhibits introduced in evidence before the Referee in the proceedings of April 26, 1940 and May 1, 1940, said exhibits being described as follows:

No. 1—Certified copy of regulations covering the re-drilling operations of wells.

No. 2—Document entitled "Easement 309, Huntington Beach".

No. 3—Memorandum.

No. 4—Agreement between the Huntington Beach Townsite Association, by the Huntington Shore Oil Company.

No. 5—Plat showing Huntington Shore Well and Bolsa Chica Well courses.

13. Injunction against Bolsa Chica Oil Corporation, et al., filed May 15, 1940.

14. Petition to have Bolsa Chica Corporation, et al., certified for contempt, filed August 22, 1940.

15. Order to Show Cause on Petition to have Bolsa Chica Oil Corporation, et al, certified for contempt, filed August 22, 1940.

16. Certificate of Contempt dated December 30, 1940.

17. Motion of Bolsa Chica Oil Corporation, et al, for an order to show cause why the Certificate of Contempt should not be dismissed, filed January 9, 1941.

18. Order to Show Cause on Motion of Bolsa Chica Oil Corporation, et al, relative to Certificate of Contempt, filed January 9, 1941.

19. Order to Show Cause in re contempt against

Bolsa Chica Oil Corporation, filed January 13, 1941.

20. Minute Order of District Judge dated January 30, 1941.

21. Order re Certificate of Contempt filed January 7, 1941.

22. Notice of Appeal, filed February 13, 1941.

23. Directions to Clerk of District Court for notification of filing of Notice of Appeal and mailing copies thereof to all parties to the judgment, filed February 13, 1941.

24. Pages 83 to 92, inclusive, of Reporter's Transcript of April 26, 1940 and May 12, 1940, of proceedings in re order to show cause on the petition of the Trustee for instructions, before the Referee.

25. Order extending time to docket appeal.

26. Statement of points upon which Appellant intends to rely in this appeal.

27. This Designation of Contents of record on appeal.

Dated: April 11th, 1941.

RAPHAEL DECHTER &
JOSEPH J. RIFKIND
By R. DECHTER
Attorneys for Appellant

Receipt of copy of the within instrument is acknowledged this 11th day of Apr., 1941.

OVERTON, LYMAN &
PLUMB
By E. RINGE

[Endorsed]: Filed Apr. 14, 1941. Paul P. O'Brien, Clerk.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 9790

GEORGE T. GOGGIN, as Trustee in Bankruptcy in the Matter of JACK DAVE STERLING, Bankrupt,

Plaintiff,

vs.

BOLSA CHICA OIL CORPORATION, et al,

Defendants.

COUNTER-DESIGNATION OF CONTENTS OF RECORD ON APPEAL BY APPELLANT

Comes now the appellant, George T. Goggin, as Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt, and in response to the designation of contents of record on appeal of appellees, files this counter-designation of contents of record on appeal to be contained in the record on appeal, in addition to the records, proceedings and documents heretofore designated by appellant and appellees:

1. All exhibits introduced in evidence in the proceedings before the Referee on September 26, September 30 and October 1, 1940;

2. All exhibits introduced in evidence in the proceedings before the Referee on April 26, 1940 and on May 1, 1940;

3. The following portions of the Reporter's Transcript of proceedings in re: Trustee vs. Bolsa

Chica Oil Corporation, of September 26, September 30 and October 1, 1940, before the Referee:

(a) Page 29, line 4 to page 30, line 2, inclusive.
(b) Page 34, line 21 to page 35, line 24, inclusive.
(c) Page 38, line 22 to page 40, line 7, inclusive.
(d) Page 40, line 14 to page 44, line 3, inclusive.
(e) Page 45, lines 8 to 21 inclusive.
(f) Page 56, lines 2 to 22 inclusive.
(g) Page 58, line 1 to page 59, line 20, inclusive.
(h) Page 59, line 24 to page 62, line 6, inclusive.
(i) Page 63, line 17 to page 64, line 2, inclusive.
(j) Page 66, line 8 to page 67, line 9, inclusive.
(k) Page 67, lines 17 to 26 inclusive.
(l) Page 159, line 12 to page 165, line 4, inclusive.

4. The following portions of the Reporter's Transcript of proceedings on hearing before the Honorable Leon R. Yankwich on January 30, 1941:

(a) Page 2, line 1 to page 3, line 15, inclusive.
(b) Page 78, line 24 to page 80, line 5, inclusive.

5. This counter-designation.

Dated: April 19, 1941.

RAPHAEL DECHTER and
JOSEPH J. RIFKIND
By R. DECHTER
Attorneys for Appellant.

[Title of Circuit Court of Appeals and Cause.]

(AFFIDAVIT OF SERVICE BY MAIL—
1013a, C. C. P.)

State of California
County of Los Angeles—ss.

E. Zaringer, being first duly sworn, says: That affiant is a citizen of the United States and a resident of the County of Los Angeles; that affiant is over the age of eighteen years and is not a party to the within and above entitled action; that affiant's business address is 633 Subway Terminal Bldg., 417 So. Hill St., Los Angeles, California; that on the 19th day of April, 1941, affiant served the within Counter-Designation of Contents of Record on Appeal by Appellant on the.....in said action, by placing a true copy thereof in an envelope addressed to the attorneys of record for said appellees, at the office address of said attorneys, as follows: (Here quote from envelope name and address of addressee.) "Messrs. Eugene Overton, Warren S. Pallette, and Donald H. Ford, Attorneys at Law, 733 Roosevelt Bldg., Los Angeles, California"; and by then sealing said envelope and depositing the same, with postage thereon fully prepaid, in the United States Post Office at Los Angeles, California, where is located the office of the attorney..... for the person..... by and for whom said service was made.

That there is delivery service by United States mail at the place so addressed, or there is a regular

communication by mail between the place of mailing and the place so addressed.

E. ZARINGER

Subscribed and sworn to before me this 19th day of April, 1941.

[Seal] JESSIE DOLFIN

Notary Public in and for the County of Los Angeles, State of California.

[Title of Circuit Court of Appeals and Cause.]

(AFFIDAVIT OF SERVICE BY MAIL—1013a, C. C. P.)

State of California
County of Los Angeles—ss.

E. Zaringer, being first duly sworn, says: That affiant is a citizen of the United States and a resident of the County of Los Angeles; that affiant is over the age of eighteen years and is not a party to the within and above entitled action; that affiant's business address is 633 Subway Terminal Bldg., 417 So. Hill St., Los Angeles, California; that on the 19th day of April, 1941, affiant served the within Counter-Designation of Contents of Record on Appeal by Appellant on the appellees in said action, by placing a true copy thereof in an envelope addressed to the attorneys of record for said appellees at the office address of said attorneys, as follows: (Here quote from envelope name and address of addressee.) "Elizabeth R. Hensel, Esq., 410

Park Central Bldg., Los Angeles, California, Wm. H. Cree, Esq., 1216 Security Bldg., Long Beach, California''; and by then sealing said envelope and depositing the same, with postage thereon fully prepaid, in the United States Post Office at Los Angeles, California, where is located the office of the attorney..... for the person..... by and for whom said service was made.

That there is delivery service by United States mail at the place so addressed, or there is a regular communication by mail between the place of mailing and the place so addressed.

E. ZARINGER

Subscribed and sworn to before me this 19th day of April, 1941.

[Seal] JESSIE DOLFIN

Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Filed Apr. 21, 1941. Paul J. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

DESIGNATION OF CONTENTS OF RECORD ON APPEAL BY APPELLEES M. M. McCALLEN CORPORATION, H. H. McVICAR, C. M. ROOD AND WILLIAM H. CREE.

Appellees M. M. McCallen Corporation, H. H. McVicar, C. M. Rood and William H. Cree, certain of the appellees in the above entitled proceedings,

designate the following portions of the record, proceedings and documents to be contained in the record on appeal, in addition to the records, proceedings and documents heretofore designated by appellant and by appellees Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson:

1. Exhibits introduced in evidence before the Referee in the proceedings of September 26, September 30 and October 1, 1940, said exhibits being described as follows:

Exhibit 3. Drilling and operating agreement between Bolsa Chica Oil Corporation and M. M. McCallen Corporation dated August 14, 1940.

Exhibit 4. Assignment of oil and gas lease dated August 14, 1940 from Bolsa Chica Oil Corporation to M. M. McCallen Corporation.

2. This designation.

Dated: April 18, 1941.

WILLIAM H. CREE
ELIZABETH R. HENSEL
By ELIZABETH R. HENSEL
Attorneys for Appellees
M. M. McCallen Corporation,
H. H. McVicar, C. M. Rood
and William H. Cree.

Received copy of the within this 18th day of April, 1941.

R. DECHTER
By H. WEBSTER
Attorney for Trustee.

Received copy of the within this 18th day of April, 1941.

OVERTON, LYMAN & PLUMB
Attorneys for Appellees
Bolsa Chica et al.

[Endorsed]: Filed Apr. 21, 1941. Paul P. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

DESIGNATION OF CONTENTS OF RECORD ON APPEAL BY APPELLEES BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLAN A. ANDERSON.

Appellees Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson, certain of the appellees in the above entitled action, designate the following of the record, proceedings and documents to be contained in the record on appeal, in addition to the record, proceedings and documents heretofore designated by appellant:

1. Order authorizing suit against Bolsa Chica Oil Corporation in the state court, filed September 20, 1940.

2. Petition (and attached exhibit) for leave to sue Bolsa Chica Oil Corporation in the state court, filed September 20, 1940.

3. Affidavits of Warren S. Pallette and Donald H. Ford attached to the motion of Bolsa Chica Oil Corporation for an order to show cause why a cer-

tificate of contempt should not be dismissed, filed January 9, 1941.

4. The following portions of the Reporter's Transcript of Proceedings in re: Order to Show Cause Re: Petition for Instructions of April 26 and May 1, 1940 before the Referee:

(a) Page 2, line 4 to page 4, line 21, inclusive.

(b) Page 24, lines 22 to 26, inclusive.

(c) Page 82, line 8 to page 83, line 1, inclusive.

5. The following portions of the Reporter's Transcript of Proceedings in Re: Trustee vs. Bolsa Chica Oil Corporation of September 26, September 30 and October 1, 1940, before the Referee:

(a) Page 2, lines 1 to 19, inclusive.

(b) Page 10, line 21 to page 24, line 14, inclusive.

(c) Page 28, lines 14 to 17, inclusive.

6. The following portions of the Reporter's Transcript of Proceedings on Hearing before the Honorable Leon R. Yankwich of January 30, 1941:

(a) Page 51, line 13 to page 82, line 3, inclusive.

7. This designation.

Dated: April 18, 1941.

EUGENE OVERTON
WARREN S. PALLETTE
DONALD H. FORD
By DONALD H. FORD
Attorneys for Appellees
Bolsa Chica Oil Corporation,
Thos. W. Simmons and
Allan A. Anderson.

Received copy of within April 18, 1941.

ELIZABETH R. HENSEL
Attorney for Certain Appellees.

Received copy of the within this 18th day of April, 1941.

R. DECHTER
By H. WEBSTER
Attorney for Trustee.

[Endorsed]: Filed Apr. 21, 1941. Paul J. O'Brien, Clerk.

[Title of Circuit Court of Appeals and Cause.]

COUNTER-DESIGNATION OF CONTENTS OF RECORD ON APPEAL BY APPELLEES BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLAN A. ANDERSON.

Appellees Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson, certain of the appellees in the above entitled action, because of the new matter contained in the counter-designation of contents of record on appeal by appellant, designate the following of the record, proceedings and documents to be contained in the record on appeal, in addition to the record, proceedings and documents heretofore designated by appellant in his original designation and in his counter-designation and in addition to the record, proceedings and documents heretofore designated by appellees M. M. McCallen

Corporation, H. H. McVicar, C. M. Rood and William H. Cree and these appellees:

1. The following portions of the Reporter's Transcript of Proceedings in Re: Trustee vs. Bolsa Chica Oil Corporation of September 26, September 30 and October 1, 1940, before the Referee:

(a) Page 54, line 22 to page 55, line 12, inclusive. Testimony of witness Earl Ross.)

(b) Page 71, line 14 to page 72, line 1, inclusive. (Testimony of witness Vernon King.)

(c) Page 74, line 1, to page 80, line 9, inclusive. (Testimony of witness Vernon King.)

(d) Page 81, lines 21 to 23, inclusive. (Testimony of witness Vernon King.)

(e) Page 170, line 4, to page 176, line 16, inclusive. (Testimony of witness Allan A. Anderson.)

(f) Page 212, line 12, to page 218, line 4, inclusive. (Testimony of witness Allan A. Anderson.)

2. This counter-designation.

Dated: April 22, 1941.

EUGENE OVERTON
WARREN S. PALLETTE
DONALD H. FORD
By DONALD H. FORD
Attorneys for Appellees
Bolsa Chica Oil Corporation,
Thos. W. Simmons and
Allan A. Anderson.

Received Counter-Designation of Contents of Record this 22nd day of April, 1941.

ELIZABETH R. HENSEL
By RITA L. STONE
Attorney for Appellees M. M. McCallen Corporation, H. H. McVicar, C. M. Rood and William H. Cree.

Received copy of the above this 22nd day of April, 1941.

RAPHAEL DECHTER
By H. WEBSTER
Attorney for Trustee.

[Endorsed]: Filed Apr. 24, 1941. Paul P. O'Brien, Clerk.

No. 9790.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE T. GOGGIN, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt,

Appellant,

vs.

BOLSA CHICA OIL CORPORATION, a corporation, THOS. W. SIMMONS, ALLAN A. ANDERSON, WILLIAM H. CREE, H. H. MCVICAR, C. M. ROOD, and M. M. MCCALLEN CORPORATION, a corporation,

Appellees.

BRIEF OF APPELLEES BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLAN A. ANDERSON.

EUGENE OVERTON,
WARREN S. PALLETTE,
DONALD H. FORD,
733 Roosevelt Building, Los Angeles,

Attorneys for Appellees, Bolsa Chica Oil Corporation, Thos. W. Simmons, and Allan A. Anderson.

Parker & Baird Company, Law Printers, Los Angeles.

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No. 9790.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE T. GOGGIN, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt,

Appellant,

vs.

BOLSA CHICA OIL CORPORATION, a corporation, THOS. W. SIMMONS, ALLAN A. ANDERSON, WILLIAM H. CREE, H. H. MCVICAR, C. M. ROOD, and M. M. MCCALLEN CORPORATION, a corporation,

Appellees.

BRIEF OF APPELLEES BOLSA CHICA OIL CORPORATION, THOS. W. SIMMONS AND ALLAN A. ANDERSON.

Jurisdiction.

The District Court was without jurisdiction to entertain this proceeding inasmuch as it is a court of limited jurisdiction and, sitting as a court of bankruptcy, cannot entertain an action of the character here involved. Our entire brief is devoted to this question.

Statement of the Case.

The appellant's statement of the case, pages 2, 3 and 4 of appellant's opening brief, is, in the main, correct. Appellees, however, wish to call the attention of the Court to the fact that the appearance of attorneys for Bolsa Chica Oil Corporation was special only [Tr. p. 92], and that the approval of the order of injunction by the appellee, Bolsa Chica Oil Corporation [Tr. p. 29] and the stipulation in open court by said appellee [Tr. p. 156] were both expressly subject to the objection to the jurisdiction of the Court. It should further be pointed out that the order of the district judge sustaining the objection of the appellees to the jurisdiction of the Court in no way finds that the attack is collateral, but, on the contrary, in his oral opinion the district judge expressly finds the attack to be direct. [Tr. p. 252.]

Statement of the History of the Case.

A great many of the matters contained in appellant's statement of the history of the case have no bearing upon the question of jurisdiction involved in this appeal in that they occurred after the injunction issued. They are derived from the certificate of contempt which was prepared by appellant and which, to a large extent, is not supported by the evidence adduced before the referee and, as a result, many of the statements have no support in fact. Much of the factual matter set forth has little, if any, bearing upon the matter at issue. In view of the fact that the district judge expressly refused to hear any evidence upon existence of a violation of the injunction, but merely heard argument on the question of jurisdiction, and examined the record of the proceedings prior to the issuance of the injunction

order, the facts occurring subsequent to the issuance of the injunctive order are not at issue in this proceeding. If they were, appellees are prepared to show from the production record of appellant's well subsequent to the replacing of the same on production that it has suffered no loss of production or damage other than the expense of replacing it upon production. Appellees dislike taking the time of the Court in a discussion of matters not directly before it, but feel that it is necessary, in view of the statements of appellant, to make a proper statement of the facts as disclosed by the record.

At the time of the institution of this proceeding appellant and appellee, Bolsa Chica Oil Corporation, were the operators, respectively, of two oil wells located at Huntington Beach, California, the tops of which oil wells were located on two separate parcels of property in the town of Huntington Beach some distance apart, both of said wells being bottomed beneath the ocean in property belonging to the State of California. [Tr. pp. 19, 44, 45, 101.] Both of said wells were operated under identical easements granted by the State of California permitting the operators to produce oil and gas from beneath the tideland. These easements give each operator a cylindrical easement, twenty-four (24) inches in diameter, through the land of the state, which easement is the only property right involved. [Tr. p. 117.] At the time of the institution of these proceedings, appellant's well was producing, but the well of Appellee, Bolsa Chica Oil Corporation, was off production due to its casing having collapsed. Both wells had produced for a number of years, both of them having been drilled prior to 1934. Each of them had been redrilled prior to this proceeding. At the time of the redrilling, referred to by appellant, of its well, it was re-

drilled in such a manner as to cause its course to come close to the location of the Bolsa Chica Oil Corporation well, which was then producing. No damage was caused by appellant to the Bolsa Chica Oil Corporation well at the time of the redrilling of appellant's well. The appellees' well subsequently went off production due to collapse of its casing, and, while Bolsa Chica Oil Corporation and its predecessor in interest had made no objection to the redrilling of appellant's well, appellant instituted this proceeding before the referee in an attempt to prohibit the redrilling of appellees' well, which attempt was successful, inasmuch as said well, due to the present proceeding, has never been completed, in spite of the expenditure of in excess of $45,000.00 by appellees in such attempt.

The redrilling operation undertaken by appellees, at all times after the injunction order was issued, was in accordance with the rules and regulations of the State of California, and expressly approved by the State of California, the owner of the property into which the two wells were drilled. Furthermore, the operations conducted by appellees were at no time contrary to the terms of the injunction made and entered by the referee, even assuming that such injunction order might have been valid. Appellant has not alleged or claimed that the appellees' well was drilled upon or collided with appellant's property or well. Appellant bases his case on the use of mud by appellees as the circulating medium. The use of mud in the redrilling of appellees' well is the customary procedure in Huntington Beach as well as elsewhere, and in accordance with the rules and regulations of the State of California, so long as such use is limited to areas above the oil bearing sands. Appellees obtained the consent of appellant's engineer to the use of mud as a circulating medium prior

to any use thereof. [Tr. p. 225.] After appellant's well was mudded off, on June 10, 1940, appellant's engineer expressly approved the continued use of mud in the cleaning out of appellees' well, and the continued use of mud in further redrilling operations of appellees' well from June 10, 1940, until July 18, 1940 [Tr. pp. 227, 195, 197], at which time appellees had drilled to the top of the oil sand and changed to oil as a circulating medium. [Tr. pp. 226, 227.] Appellees at no time improperly used mud when drilling in the oil sand, or at any time after the injunction, without the consent of appellant's authorized agent.

The redrilling of wells in Huntington Beach field is a common and usual practice and it is impossible to redrill such wells without using mud as the circulating medium. (In drilling an oil well, a fluid, usually special types of clay and water (mud) is circulated through the drill pipe for three reasons: (1) to remove from the hole the material cut by the drill; (2) to lubricate the drill pipe; and (3) to maintain a cap or weight to counter-balance the gas pressure in the formation. If a well is drilled close to a producing well, there is a possibility that the drilling mud may pass through the producing formations into the neighboring well. In this event, such neighboring well may temporarily be shut down while the mud is cleaned out, or such mud may be pumped out in the usual course of pumping operations.) Many such wells have been redrilled without damage to adjoining wells. The damage to appellant's well in this case was largely contributed to, if not wholly caused by, appellant's own actions in failing to

stop pumping its well during such time as appellees were drilling in the proximity of appellant's well. [Tr. p. 185.]

In the latter part of July, 1940, after appellee, Bolsa Chica Oil Corporation, had drilled several hundred feet into the oil sand and was about to complete its well, due to the condition of the structure and the use of oil as a circulating medium, the well caved in and it was, therefore, necessary, in order to complete the same, to back up, recommence drilling above the oil sand, and use mud as a circulating medium. [Tr. p. 231.] Appellees asked the permission of appellant's engineer, in accordance with the terms of the injunction, to change back to mud. This permission was refused. Rather than violate the injunction, even though it was believed to be void, appellee, Bolsa Chica Oil Corporation, sold the well to appellee, M. M. McCallen Corporation [Tr. p. 202], which thereupon took over the well and cleaned out and surveyed the well. M. M. McCallen Corporation conducted no drilling operations, although it did use mud to circulate the well while cleaning it out to its then bottom far above the oil sand and in surveying its course. These operations were suspended shortly after the service of the contempt citation and upon completion of surveying operations, and have not been recommenced.

The above facts, to the extent the Court cannot take judicial notice thereof, *People v. Associated Oil Co.*, 211 Cal. 93, 105; *Gilbreath v. States Oil Corp.* (C. C. A. 5th), 4 Fed. (2d) 232, are supported by the record, and this statement is made to disabuse the mind of the Court of the impression to be gained from appellant's statement of the history of the case that there was a violation of the injunction and an intentional disregard of the order of the referee.

Questions Involved in This Appeal

1. Does a referee in bankruptcy have the power to enjoin, in a summary proceeding, without consent, or at all, the drilling of an oil well in a lawful manner without negligence by and on property of a third person, a stranger to the bankruptcy proceeding?

2. May not the invalidity of the order of injunction of the referee be shown upon hearing of the referee's certificate of contempt for alleged violation of such order, in the same bankruptcy proceeding and Court, when such order was made in excess of the jurisdiction of the referee?

3. Upon direct attack on the validity of such order of the referee, may not error be shown in the making of such order as well as excess of jurisdiction, lack of jurisdiction or failure to exercise jurisdiction in the proper manner?

4. Does the act of stipulating that an order may be entered by the referee upon the express condition that the person so stipulating reserves his objections to jurisdiction, timely made, prevent him from showing the lack of jurisdiction of the referee to make such order, on hearing of the certificate of contempt for alleged violation of such order?

5. May consent be given to the entry of an order in excess of the jurisdiction of the referee which will preclude the raising of such lack of jurisdiction, on hearing of the certificate of contempt for alleged violation of such order in the same bankruptcy proceeding and same district court?

ARGUMENT

I.

The District Court Had No Jurisdiction To Make the Order of Injunction Which Is, Therefore, Invalid and Void, and the District Court Did Not Err In Dismissing The Contempt.

1. The Injunction Prohibiting Appellee From a Normal and Lawful Use of Its Property, Was Beyond the Jurisdiction of Any Court.

2. The Order of Injunction Was Beyond the Jurisdiction of the District Court.

The facts indicate that appellee, Bolsa Chica Oil Corporation, an operator in the same oil field as appellant, was about to redrill and deepen an oil well from a town lot drilling site, not adjacent to, but in the neighborhood of the town lot drilling site of appellant. Appellant conceived the possibility that this operation might result in harm to its well.

Anticipating that appellee Bolsa Chica Oil Corporation, might in its drilling operations, mud off appellant's well, appellant applied for and was given an injunction by the referee in bankruptcy, which is the basis of the present contempt proceedings.

It is our contention that such act was in excess of the jurisdiction of the referee, and that had such an application been made to any court, such an injunction would have been in excess of its jurisdiction.

Jurisdiction is a word that has been given so many various meanings that its particular use in a given instance needs definition. We propose here to discuss jurisdiction as it involves the power of the court, it being our

belief that no court, under the facts of the case at bar, has jurisdiction to grant an injunction. Illustrative of the lack of the type of jurisdiction that we believe here exists is the following explanatory statement on jurisdiction found in 28 Am. Jur. 423 reading as follows:

> "Under constitutional provisions which confer power upon certain courts to issue writs of injunction and all writs necessary to enforce their jurisdiction, and statutes which in broad terms provide for cases in which injunction may issue, such courts may issue writs of injunction in all cases in which courts of chancery would have power to issue them conformably to established rules of equity. The legislature may change the substantive law and in so doing increase or reduce the subject matter upon which the jurisdiction of courts to issue injunction operates.
>
> Jurisdiction, in this connection, does not relate to the right of the parties as between each other, but to the power of the court. The question of its existence is an abstract inquiry, not involving the existence of an equity to be enforced, or the right of the plaintiff to avail himself of it if it exists. It precedes these questions, and a decision upholding the jurisdiction of the court is entirely consistent with a denial of any equity, either in the plaintiff or in anyone else. It exists, in such sense as to render injunction obligatory, when the court granting it has authority to decide whether the application for it shall be granted —it does not depend on the correctness of the decision. Courts sometimes say that there is no jurisdiction to award injunction, when they mean merely that equity ought not to give the relief asked. In other words, they are referring rather to a lack of sufficient grounds for issuing the writ than to want of power. The distinction should be kept in mind between total

> want of jurisdiction—absolute absence of power to entertain the injunction suit and award the remedy—and an unjustifiable or erroneous exercise of jurisdiction. A proper understanding of these two phases of jurisdiction is necessary in determining the validity and binding effect of the injunction decree and its vulnerability to collateral attack."

In the present case an injunction was issued on the mere apprehension of injury. No injury was threatened, no invasion of appellant's property was imminent. The proceedings that culminated in the injunction were unusual to say the least. Appellant, an oil operator in a common pool, hailed a fellow operator into court and asked that the court instruct this fellow operator as to the use he might make of his property. There was no claim that the fellow operator was violating any law, or that he was using his property or was about to use his property in an unlawful manner. There was no charge of negligence. There was no claim that appellee was about to perform any act in redrilling its well that was not the usual or customary practice in the industry. Yet appellee was brought into court and was subjected to a broad injunction which virtually gave to appellant control of appellee's drilling operations.

In short, one property owner was permitted to control and to dictate his neighbor's use of his property. Appellant claims no property interest in appellee's property. Appellant points to no statute that makes appellee's property subservient to appellant. There is no common law principle that would justify its assertion of dominion over its neighbor. No nuisance was involved. No right of appellant was invaded or even threatened. We submit that a monstrous wrong was done to appellee; private rights

were ruthlessly invaded and the referee in bankruptcy exceeded his power in granting such an injunction. He purported to enjoin acts of appellee concerning which no court had authority to invade by injunction.

This is not a situation where it may be said that the referee was simply acting to protect the property of the bankrupt estate. He was not so acting. He was supervising appellee's use of its property, under the guise of protecting appellant's property.

If a referee in bankruptcy can tell appellee how to conduct its drilling operations, he can likewise supervise all other neighboring operators, and as it is common knowledge that due to the fugacious character of oil and gas, what one operator does in a field to a greater or less degree affects all operators in the field, it follows that a referee under the disguise of protecting bankrupt assets, may control an entire oil pool. Such is not the law.

It would be absurd to contend that by the scheme of injunction, or on the theory of protecting property in the custody of the court, a trustee in bankruptcy of an estate that had as an asset a motor vehicle, if a third person was involved in an accident with this motor vehicle, could hold in contempt of court and for damages in a contempt proceeding, such third person. The possibility of being involved in an automobile accident is as imminent as damage from drilling. Because there have been automobile accidents, can a referee enjoin all residents of a district from having an accident involving bankrupt property? May he by injunction, dictate driving speeds for others, the type of gasoline used, the kind of tires, and the like? And may he, in the event of accident, hold third persons guilty of contempt and assess damages, denying a jury

trial, and ignoring all questions of negligence on the part of such other person and contributory negligence on the part of the operator of the trust estate vehicle? Such in legal effect is appellant's case.

Illustrative of our contention as to our right to the lawful use of our property without interference from third persons, see:

22 Cal. Jur. 419;

Hoffman v. Tuolumne County Water Co., 10 Cal. 413 (1858);

Sutliff v. Sweetwater Water Co., 182 Cal. 34 (1920).

Equity will not restrain a property owner from a lawful use of his property.

American Bank & Trust Co. v. Federal Reserve Bank of Atlanta, 67 L. Ed. 1153, 262 U. S. 643 (1922);

City of Janesville v. Carpenter, 77 Wis. 288, 46 N. W. 128, 8 L. R. A. 808 (1890).

See also:

Beauchamp v. United States, 76 Fed. (2d) 663 (C. C. A. 9th, 1935);

Vallely v. Northern F. & M. Ins. Co., 254 U. S. 348, 65 L. Ed. 297 (1920).

In *American Bank & Trust Co. v. Federal Reserve Bank of Atlanta, supra,* plaintiff sought to enjoin the Federal Reserve Bank, by offering superior facilities for clearing of checks. In so doing, the Federal Reserve Bank subjected country banks to losses. (Elimination of discounts and by speed in clearance, loss of interest.) Plain-

tiff sought to enjoin the Federal Reserve from so acting. The court said:

> "Country banks are not entitled to protection against legitimate competition. Their loss here shown is of the kind to which business concerns are commonly subjected when improved facilities are introduced by others, or a more efficient competitor enters the field. It is *damnum absque injuria.*"

The injunction was denied.

Mr. Justice Brandeis' language is equally applicable here. If, as a result of a lawful non-negligent use of our property, plaintiff was damaged, it would have been *damnum absque injuria.* Under such circumstances a plaintiff, because he anticipates the possibility of a loss for which the law gives him no remedy, cannot by the device of an injunction, create a right that otherwise is nonexistent in the law.

This is strikingly illustrated by the case of *City of Janesville v. Carpenter, 77* Wis. 288, 46 N. W. 128, 8 L. R. A. 808 (1890). The City of Janesville and Janesville Cotton Mills sought to enjoin defendant from erecting a building on Rock River on property owned by defendant. The building would involve the driving of piling. The theory of plaintiff city, when reduced to its fundamentals, was that if defendant so built, other persons might follow his example, and when similar buildings extend up and down the river, danger by fire and flood, and to the public health would result. The theory of the Janesville Cotton Mills was that the erection would cause the water of the river to rise and set back to some extent at the place where the mill took its water. There was no evidence that this would be harmful.

As to the city's contention the court said:

> "This is a most remarkable case, and there has never been anything like it. It is not charged that the proposed building will in itself do any harm in any respect whatever, or that the defendant has not the right to build it where he proposes to build it, but that it may possibly be followed as an example by others in building buildings which may possibly do harm. It would be a new case where one had actually done something in itself right and harmless, and he should be sued, because others had done something wrong and injurious by following his example, and it would be a strange case to enjoin one from doing something right and harmless in itself, because others may possibly do something wrong and injurious by following his example; and yet the latter is the present case. A mere example is not actionable. Such is the action in favor of the City."

Concerning the *Janesville Cotton Mills* case the court said:

> "We think the learned counsel of the appellant is right in claiming that the complaint does not charge facts sufficient to state any cause of action known to the general laws of the land and the practice of courts in favor of either plaintiffs. But, even if the complaint sufficiently charged that the consequences predicted would be produced by the proposed building, the City of Janesville has no such corporate interest in them as would authorize it to maintain such an action. *Milwaukee v. Milwaukee & B. R. Co.,* 7 Wis. 85; *Sheboygan v. Sheboygan & F. du L. R. Co.,* 21 Wis. 668.
>
> But it is sufficient that no wrong, injury or damage is charged. By the extended jurisdiction of the

court in equity, by chapter 190 of the Laws of 1882 amending section 3180, Rev. Stat., there must be some special injury or necessity to protect the rights of some person, to grant an injunction. As a private nuisance or a public nuisance, by which some private person has suffered some special and peculiar injury, there must be material annoyance, inconvenience, discomfort or hurt, and the violation of another's rights in an essential degree. Wood, Nuis. 1-4.

The law gives protection only against substantial injury, and the injury must be tangible, or the comfort, enjoyment or use must be materially impaired. *Stadler v. Grieben,* 61 Wis. 500; *Pennoyer v. Allen,* 56 Wis. 502, and many other cases in this court.

It is a maxim of the law that wrong without damage or damage without wrong does not constitute a cause of private action. It is charged that this building will be in violation of an ordinance of said City. That would not give a cause of action for an injunction, even if the ordinance so provided. *Waupon v. Moore,* 34 Wis. 450.

The argument of the learned counsel of the respondents, and the authorities cited on the question whether the proposed building will obstruct the navigation of the river, are impertinent to the case. There is nothing in the case that involves any such question in the remotest degree. Within any grounds or reasons known to the well-settled principles and practice of equity jurisprudence, the complaint states no case for an injunction, or for any other purpose. The action is not based on any statute which gives a right of action in such a case. But the learned counsel of the respondent cites chapter 423, Laws 1887, in support of the action. This Statute is, if possible more marvelous than the complaint."

The court then proceeds to hold the statute unconstitutional as special legislation.

In the present case there was no wrong threatened on which appellant was entitled to damages, and damage without wrong does not constitute a cause of private action. Where such are the facts, a complaint cannot state a cause of action for an injunction—the court lacks jurisdiction. Appellant here, by the guise of injunction and the remedy of civil contempt, is seeking damages under facts where the law denies it damages. It is seeking to establish a principle of liability without fault to circumvent the law by its scheme of an injunction.

An analogous case is *Beauchamp v. United States,* 76 Fed. (2d) 663, which establishes the law in this, the 9th Circuit.

There, a referee in bankruptcy, following a trustee's sale of the business of the bankrupt estate, an insurance agency corporation, enjoined Beauchamp and his sons who had owned all but qualifying shares of the corporation, from reengaging in the same business, from competing with the purchaser and from soliciting former customers and patronage. It was held by this court as follows:

> "Appellant was under no contractual obligation to refrain from soliciting customers of the former business of which he was an agent. The right to use his own name in earning a livelihood should not be taken away. While a covenant not to solicit can be implied in a voluntary transfer, there is no such implication in an involuntary transfer. The policy of the Bankruptcy Act to give the bankrupt a fresh start in life would be defeated if he were precluded from engag-

ing in a similar business or from soliciting his old customers. Were the policy of our bankrupt statutes otherwise, instead of being a mode of relieving the debtor, it would close to him every avenue of hope for the future. *Helmbold v. Henry T. Helmbold Mfg. Co.,* 53 How. Prac. (N. Y.) 453; *Theobald-Jansen Electric Co. v. Harry I. Wood E. Co.,* 285 F. 29 (C. C. A. 6); *Bellows v. Bellows,* 24 Misc. 482, 53 N. Y. S. 853.

The order of the referee appears invalid, for the reason that it is permanent, extends to all business, and is not restricted to any particular locality. The Code provides that: 'One who sells the good-will of a business may agree with the buyer to refrain from carrying on a *similar* business within a *specified county, city,* or *a part thereof,* so long as the buyer, or any person deriving title to the good-will from him, carries on a like business therein.' (Italics ours.) Civ. Code Cal., Sec. 1674.

In order that disobedience of this injunction order may constitute contempt, it is necessary that the order be valid. Disobedience of a void mandate, order, judgment, or decree, or one issued by a court without jurisdiction of the subject-matter and the parties litigant, is not contempt.

When '* * * a court of the United States undertakes, by its process of contempt, to punish a man for refusing to comply with an order which that court had no authority to make, the order itself, being without jurisdiction, is void, and the order punishing for the contempt is equally void. * * *' *Ex parte Fisk,* 113 U. S. 713, 5 S. Ct. 724, 726, 28 L. Ed. 1117; *Ex parte Terry,* 128 U. S. 289, 9 S. Ct. 77, 32 L. Ed. 405; *In re Ayers,* 123 U. S. 443, 8 S. Ct. 164, 31 L. Ed. 216."

There as here, an order was made in excess of the jurisdiction of the referee and it was there held that contempt cannot be predicated on an order where such jurisdiction is lacking.

As a summary to this point we desire to quote from the oral opinion of the Honorable Judge Leon R. Yankwich in the court below:

> "This order, in addition to enjoining the defendants, also gave authority to the trustee to institute action for damages or for injunctive relief. They were brought here on a contempt citation and it was insisted that the court penalize them for the violation of this injunction of the court. In other words, the court has power to impose a fine and impose it by way of damages, then allow the estate later on to assess additional damages for the loss caused by the acts themselves after the court had imposed the penalty for violation of its interdict. The courts lately have scrutinized records and have raised questions relating to jurisdiction when the thought never occurred to counsel and was never even suggested by counsel to the court below. I feel, in a case of this character, where the challenge over jurisdiction has been made, the court should inquire into it. I am satisfied that the court has no jurisdiction whatsoever and that their appearance and response to an order to show cause, which they have to obey under penalty of having default taken against them, didn't constitute a waiver. And if, as I believe, it is beyond the power of the bankruptcy court to, in effect, make a declaration that unless the well is drilled in a certain way damage will result and the man will be enjoined from doing something on his

> own property, property which is not the subject of bankruptcy, his actions therein, in the failure to review, does not involve a waiver on his part."

We have heretofore discussed the question of jurisdiction from the aspect of any equity court, and have contended that no court has jurisdiction to enter the injunction order here for review. We desire briefly to consider the special question of the jurisdiction of a Federal District Court, and of its Referee, as it applies to the facts of the case.

The District Court is a court of limited jurisdiction. (*Simkins' Federal Practice*, 3d Ed., Sec. 23, p. 36; 28 *U. S. C. A.*, Sec. 41 (1).)

There is no presumption in favor of jurisdiction, but on the contrary the presumption is against jurisdiction, and jurisdiction must affirmatively appear on the face of the record in order to vest the court with jurisdiction. (*Simkins' Federal Practice,* 3d Ed., Sec. 26, p. 38.)

The burden of establishing the jurisdiction is upon plaintiff, and it never shifts. (*Simkins' Federal Practice,* 3d Ed., Sec. 29, p. 43.)

Objection to the jurisdiction may be raised at any stage of the proceeding. (*Simkins' Federal Practice*, 3d Ed., Sec. 27, p. 38.)

Under the Constitution of the United States, there must be an actual existing factual controversy, and no advisory opinion may be rendered by the Federal courts. (*Simkins' Federal Practice,* 3d Ed., Sec. 24, p. 37, citing cases.)

It follows from the above that it is incumbent upon the appellant to establish from the record affirmatively the existence of the jurisdiction of the referee in the proceeding. The rule is well stated in 20 *American Jurisprudence,* Sec. 31, p. 224, as follows:

> "It would seem to follow, and in fact has become an established principle of equity, that one may not be enjoined from doing lawful acts to protect or enforce his rights of property or of person even though damage or loss may result to another as a necessary consequence thereof."

The mere fact then that appellant may have suffered damage is not *ipso facto* sufficient as a ground for vesting the Court with jurisdiction to have issued an order of the character here involved. That which appellees have done has not been shown to be an unlawful, wilful, negligent or unreasonable use of their property, or a nuisance, or anything else than customary and ordinary oil field practice in the field in which the property is located. It is the contention of appellees that no right of action of any nature or character to recover damages exists in appellant in the absence of a showing of negligence or intentional injury, which has not been alleged or proven.

The order of the referee did not enjoin appellees from trespassing upon the property of the bankrupt. It affirmatively prohibited them from taking a particular course in the drilling of their well, and from the use of certain

materials in connection with such drilling. There is no allegation that appellees approached closer to the well than the prohibited distance. The only allegation is that appellees used mud as a circulating medium contrary to the terms of the injunction, which is a fact appellees contend is not the case, and cannot be proven, even if the injunctive order were valid.

If the appellant is predicating his case upon the general equity jurisdiction of the District Court, it is obvious that no such jurisdiction existed for the following reasons:

1. No diversity of citizenship between the parties was alleged or appears from the record.

2. There is no allegation of inadequacy or uncertainty of damages.

3. There is no allegation of continuous trespass.

4. There is no allegation of the existence of a nuisance.

5. There is no allegation of an unlawful act.

6. There is no allegation of the insolvency of appellees.

7. There is no civil liability for the damage suffered under any circumstances.

All of the cases cited by appellant in his brief, dealing with the power to issue injunctions, are based upon one or more of the above grounds. Appellant has filed suit for damages in the Superior Court of the State of California, which is now pending. If appellant is entitled to any dam-

ages, he will recover them in that action. It is the contention of appellees in that action, as well as in this proceeding, that there is no liability in any event in the absence of negligence.

If, as heretofore considered, appellant is relying upon the bankruptcy jurisdiction of the Court, it is equally obvious that there is no jurisdiction, inasmuch as the bankruptcy jurisdiction is limited to enjoining trespass upon, or interference with the possession of property belonging to, and in the custody or possession of the bankruptcy estate. All of the appellant's cited cases on this point show, upon the facts and in the quotations, that the power is so limited. In no case which the appellant has cited, or which we have found, has the District Court under the bankruptcy jurisdiction enjoined a stranger to a bankruptcy proceeding from making a lawful use of his own property which is not in the possession, custody or control of the bankruptcy court.

We submit, therefore, that there was no jurisdiction for the action of the referee in issuing an injunction such as here before the Court. In so doing he exceeded his power as an arm of the Federal District Court. We have shown that no court of equity possesses the jurisdiction to make such an order and that Federal courts, being courts of limited jurisdiction, certainly have no such jurisdiction, and that even if they had, in the present case so many other jurisdictional factors are absent that the injunction was wholly void.

II.

The Referee Had No Jurisdiction to Make the Order of Injunction in a Summary Proceeding, Which Order Is Therefore Invalid and Void.

Whether or not plenary jurisdiction existed in the District Court, the referee is without power or authority, in a summary proceeding, to enjoin a stranger to the bankruptcy from performing a lawful act upon his own property. The jurisdiction, in this connection, of the referee, is stated as follows at 8 *Corpus Juris Secundum* 981:

> "The jurisdiction and authority of a Referee in Bankruptcy under a general reference is limited to ordinary administrative proceedings in bankruptcy and such controversial matters as arise therein and are in effect a part thereof. He is without jurisdiction to pass on issues raised in a plenary suit by the trustee against a third party to set aside a fraudulent transfer or conveyance and affecting property not in the custody or control of the court of bankruptcy.
>
> A Referee cannot entertain an action to collect a debt or a suit for specific performance."

An examination of the authorities collected in 8 *Corpus Juris Secundum,* page 982, indicates that the referee's power to issue injunctions is limited to enjoining interference with the trustee's possession of property in his control. The only case whch we have found dealing with injunctive power over property not in the possession or control of the bankruptcy is *In re Ward,* 104 Fed. 985 (Dist. Court, Mass.). In this case the referee attempted

to enjoin disposition by a third party of property claimed by the bankruptcy estate but in the possession of such third party. The Court held that the referee was without jurisdiction to order such injunction due to his lack of power to recover possession. The so-called turn-over cases, by analogy, are practically conclusive on the limited nature of the referee's summary jurisdiction. As was said in *In re Meiselman* (C. C. A. 2nd), 105 Fed. (2d) 995:

> "It is now settled that, if there is a real and substantial controversy of law or fact as to property held adversely to a bankrupt * * * the bankruptcy court is 'without jurisdiction' to adjudicate the matter but the trustee must have resort to a plenary suit."

Similarly, in *Harrison v. Chamberlain,* 271 U. S. 191, 70 L. Ed. 897, 46 S. Ct. 467, which involved a summary proceeding to determine title to property held by a stranger to a bankrupt estate, the Court held that, if there is any substantial question of law or fact, even if fraudulent, it must be determined in a plenary action. In this case the defendant objected to the jurisdiction, was overruled, and then answered, which action did not estop him from later objecting to the summary jurisdiction.

A similar case is *Weidhorn v. Levy,* 253 U. S. 268, 64 L. Ed. 898, 40 S. Ct. 534, which case contains a very good discussion as to the difference between a bankruptcy "proceeding" and a "controversy." This case holds that the referee is merely an officer

of the Court and has no power in the absence of consent to determine adverse claims.

A similar case, which is cited and discussed in *Matter v. Baldwin,* 291 U. S. 610, cited and relied on by appellant at page 46 of his brief, is *Taubel-Scott-Kitzmiller Co. v. Fox,* 264 U. S. 426, 68 L. Ed. 770, 44 S. Ct. 396. This case involved a summary proceeding to declare void a lien on property in possession of the sheriff and not the trustee. The Court held that there was no jurisdiction in the referee, either summary or plenary, to make such declaration. The Court says, at page 438:

> "Neither the judgment creditor nor the sheriff had become a party to the bankruptcy proceeding. There was no consent to the adjudication by the bankruptcy court of the adverse claims. The objection to the jurisdiction was seasonably made and was insisted upon throughout. The bankruptcy court, therefore, did not acquire jurisdiction over the controversy in summary proceedings, nor did it otherwise."

Proceedings before the referee are informal and require no formal pleadings defining the issues in controversy. It would be hard to find a better example of the injustice which would result from extending the jurisdiction of the referee than is present in this case. Appellees believe, and contend that there is no liability of any character under the circumstances, which contention they will have an opportuinty to sustain under well established rules of procedure in the Superior Court of the State of California in the action now pending therein filed by ap-

pellant. If the referee, upon informal proceedings arising on a petition for instructions, with only a few days' notice, with no issues defined, and involving a highly technical engineering matter which might easily be the subject of protracted litigation requiring the testimony of highly skilled technical engineers, has authority to enter an injunctive order of the character involved in the case at bar, violation of which submits the appellees to civil damages, where no legal liability or fault exists, the miscarriage of justice is so apparent as to be obvious.

To summarize, the appellees contend:

1. That there is no liability of any character under the circumstances in the absence of alleged and proven fault, which has not been done.

2. There is no injunctive power in any court upon the facts at bar.

3. Even if fault were alleged and could be proved, and even if there were power to issue an injunction in the State court, the Federal court has no such power, because the case is not within either the equity or bankruptcy jurisdictions of the District Court.

4. Even if all of the contentions above made could not be sustained, the referee has no summary jurisdiction to issue the order, violation of which is complained of by the appellant in the absence of consent by appellees, which consent was not given, as hereinafter in this brief is conclusively shown.

III.

The Invalidity of the Order of Injunction May Be Shown on the Hearing on the Certificate of Contempt and the District Court Did Not Err in Permitting the Attack and Dismissing the Contempt.

1. The Attack Was a Direct Attack, and Hence, Whether the Order Is Void on Its Face or Merely Erroneous, the District Court Properly Dismissed the Contempt Proceeding.

2. Even if the Attack Was Collateral, It Could Be Made, as the Order of Injunction Was Void on Its Face as Beyond the Jurisdiction of the Court to Make.

3. In Any Event, the District Court Has Power to Vacate or Modify Its Orders in Bankruptcy at Any Time During the Pendency of the Bankruptcy Proceeding, and the Order of the District Court Dismissing the Certificate of Contempt and Impliedly Vacating the Order of Injunction Was Validly Made and Is Conclusive on Appeal in the Absence of Abuse of Discretion.

Whether the attack is direct or collateral, lack of jurisdiction being apparent on the face of the record, the question as to whether or not the appellees may raise on contempt proceedings the question of the authority of the referee to render the injunction will stand or fall with the determination of the Court of the first point made in this brief that the referee had no jurisdiction to make the order. (21 *Corpus Juris Secundum,* Sec. 116, p. 177.) That is to say, if the referee had jurisdiction, this appeal is determined adversely to appellees in any event (unless the decision of the District Court is conclusive as hereinafter pointed out); if the referee did not have jurisdic-

tion, such lack of jurisdiction being apparent from the face of the record, whether the attack may be said to be direct or collateral, it may be raised at the hearing upon the certificate of contempt and this appeal is determined adversely to appellant.

It hardly needs further argument than the mere statement above made that, under the circumstances here involved, the question of the nature of the attack is immaterial and the determination thereof is merely ancillary to the determination of the main question as to whether or not the referee had jurisdiction to make the order. In view of the fact, however, that this is the point upon which appellant mainly relies, rather than lack of jurisdiction itself, and the one to which he has devoted the major portion of his brief, it is well to discuss in general the cases cited by him, and upon which he relies, even though his theory of the case is erroneous.

It should be pointed out at the start that appellant has not directed the attention of the Court to any case involving a situation similar to that at bar. He has not cited a single case arising on a contempt proceeding in the same bankruptcy proceeding as that in which the order violated was issued. Whether this is because he was unable to find any such case, or whether he studiously avoided them, we are unable to say. In any event, he is forced to argue by analogy, from cases citing the hornbook rule, that a collateral attack may not be made upon a judgment unless it is void on its face. Every case cited in appellant's opening brief, with possibly one exception, involved two distinct proceedings. The attack in each instance was made in a separate action upon a judgment or order obtained in a prior action; hence, the attack was obviously

collateral. The exception is the case of *Robert H. Jackson v. Irving Trust Co., et al.,* 85 L. Ed. Adv. Op. 310. That case arose on motion to vacate. The Circuit Court held the attack collateral. The Supreme Court does not find it necessary to do so. It says (p. 313), "The suit in question was precisely within the terms of the Act." That case was merely an attempt to retry all the issues of the prior proceeding. It was not a contempt proceeding and does not apply to the problem at bar even by way of analogy.

The appellant is relying, as above stated, solely on analogy and general language used by the courts in discussing the ordinary rule of collateral attack. Appellees are not, but on direct authority. The District Judge, in rendering his decision in this case, expressly stated that the attack in this case is a direct attack and not a collateral attack. He pointed out that it is inherent in a contempt proceeding arising in the same bankruptcy proceeding in which the order of injunction is made, that the attack is by its very nature direct and not collateral. In taking this view, he relied upon the leading case of *Ex parte Sawyer,* which he discusses in his opinion [Tr. pp. 253 to 259], and which fully substantiates his view. In addition to this case, the leading case on the subject which has been cited in a number of instances is *Ex parte Fisk,* 113 U. S. 713, 28 L. Ed. 1117, 5 S. Ct. 724, which expressly holds that the matter of the validity of the original order may be raised in a contempt proceeding, arising by virtue of violation of such order, and if the order is void for lack of jurisdiction, the defendant may not be held in contempt. In this case the Federal Court directed defendant to submit to examination. He refused and was committed for

contempt. The case arises on writ of *habeas corpus*. While, under some circumstances, the Court had the right to order an examination, it was found that they were not present in this case, and, hence, the order was beyond the power of the Court to issue. The Supreme Court examined the record to ascertain this fact. The *Fisk* case is relied upon by the Circuit Court of Appeals of the Ninth Circuit in determining, in 1935, the case of *Beauchamp v. United States,* 76 Fed. (2d) 663, referred to hereinbefore. In this case, an order to show cause was issued by the referee in bankruptcy requiring the respondent to appear before the referee to show cause why he should not be enjoind from competing with the insurance business thertofore conducted by the bankrupt corporation of which he was stockholder. The referee enjoined the servants and employees of the bankrupt from doing certain proscribed competitive acts. The respondent subsequently performed certain of the proscribed acts, and the contempt proceedings were thereupon brought. The defendant demurred to the information in the contempt proceeding and was overruled, was found guilty and fined. The Circuit Court found that the order of the referee was invalid for the reason that it was permanent, extended to all business, and was not restricted to any particular locality, and hence, in excess of the jurisdiction of the Court. The Court then goes on to say:

> "In order that disobedience of this injunction order may constitute contempt, it is necessary that the order be valid. Disobedience of a void mandate, order, judgment, or decree, or one issued by a court without jurisdiction of the subject-matter and parties litigant, is not contempt.

> "When '* * * a court of the United States undertakes, by its process of contempt, to punish a man for refusing to comply with an order which that court had no authority to make, the order itself, being without jurisdiction, is void, and the order punishing for the contempt is equally void. * * *' *Ex parte Fisk*, 113 U. S. 713, 5 S. Ct. 724, 726, 28 L. Ed. 1117; *Ex parte Terry*, 128 U. S. 289, 9 S. Ct. 77, 32 L. Ed. 405; *In re* Ayers, 123 U. S. 443, 8 S. Ct. 164, 31 L. Ed. 316."

This case is squarely in point, and being decided by the Ninth Circuit, is determinative of this appeal. That the question of collateral attack was considered and determined is clearly shown by Justice Wilbur's concurring opinion.

Now, turning to the case upon which appellant principally relies, to-wit: *Stoll v. Gottlieb*, 305 U. S. 165, 83 L. Ed. 104, 59 S. Ct. 134, we find the same distinction made. The Court at page 176, in distinguishing the case of *Vallely v. Northern F. & M. Insurance Company*, 254 U. S. 348, 65 L. Ed. 297, 41 S. Ct. 116, states as follows:

> "The case is also distinguishable because the motion to vacate was made in the same bankruptcy proceeding as the order."

In other words, *Stoll v. Gottlieb* involved two distinct proceedings and, hence, the attack was collateral. Justice Reed obviously had in mind the fact that if the attack arose in the same proceeding, still pending, in which the order had been issued, the attack would be direct inas-

much as, in bankruptcy, orders may be modified, vacated or set aside at any time until the close of the particular bankruptcy proceeding.

> *Re Cadillac Brewing Co.* (C. C. A. 6th), 102 Fed. (2d) 369;
>
> *Wayne United Gas Co. v. Owens Illinois Glass Co.*, 300 U. S. 131, 57 S. Ct. 382, 81 L. Ed. 557.

In addition,

> "When a court has erroneously exercised jurisdiction which it did not possess, it has power to correct any wrong which may have resulted from such improper action by undoing what was done, as by setting aside any ruling, order or judgment made by it, at least so long as the subject of the controversy is in its custody and the parties are before it." (21 *Corpus Juris Secundum*, p. 179, Sec. 119.)

The principal bankruptcy proceeding in which this matter arises has been pending since 1935 and is still pending with no particular imminence of termination.

The case of *Vallely v. Northern F. & M. Insurance Company*, *supra*, discussed by Justice Reed, involved a case in which an insurance corporation was adjudicated an involuntary bankrupt in the teeth of the provisions of the Bankruptcy Act excepting insurance corporations therefrom. After the time for review of the adjudication had expired, the bankrupt filed a motion to vacate the adjudication, which was upheld by the Court. Quoting from the case of *Stoll v. Gottlieb, supra*, at page 176, in this connection:

> "It was pointed out that a determination of a jurisdictional fact, such as whether an alleged bankrupt is a farmer, binds, but that where there was no

> statute of bankruptcy applicable 'necessarily there is no power in the District Court to include', the excepted corporation. It was thought that to recognize the binding effect of the judgment would be to extend the jurisdiction."

In other words, the case upon which appellant principally relies, on its face shows that it is distinguishable from the case at bar, inasmuch as it distinguishes a case on all fours with the case at bar holding that in the same proceeding an attack may be made after the time for review or appeal has elapsed on the validity of an order made in excess of the jurisdiction of the Bankruptcy Court.

Collier on Bankruptcy, 14 Ed., Vol. 1, page 146, in discussing *Stoll v. Gottlieb,* says:

> "Of course, in every case, the issue may be raised by proper direct attack in the district court or by appeal."

In support of this statement he cites *Davis v. Shackleford* (C. C. A. 8th), 91 Fed. (2d) 148, in which the court says:

> "It is true, as contended by appellees, that want of jurisdiction may be raised in the Federal Court at any stage of the proceeding * * *."

It is the contention of the appellees that, as was decided by the District Judge, where an attack is in the same proceeding, as in the case at bar, and as in the *Vallely* case, the attack is direct and not collateral. No authority has been cited by the appellant to the contrary, and the conclusion of the District Court is directly supported by the authorities herein set forth. Therefore, even if the injunction order were not void on its face, it can be at-

tacked in this proceeding on the ground of erroneous assumption of jurisdiction.

This conclusion is supported by the following additional cases:

Ex parte Lennon, 166 U. S. 548, 41 L. Ed. 1110, 17 S. Ct. 658;

Ex parte Rowland, 104 U. S. 604, 26 L. Ed. 861;

Abbott v. Eastern, etc. Co., 19 Fed. (2d) 463, (C. C. A. 1st);

Swartz v. United States, 217 Fed. 866 (C. C. A. 4th);

Brougham v. Steam Navigation Co., 205 Fed. 857 (C. C. A. 2d);

In re Home Discount Co., 147 Fed. 538 (Dist. Ct. Ala.);

In re Weiser, 19 Fed. Supp. 786 (Dist. Ct. N. Y.).

In *Ex parte Rowland, supra.* which case arose on an application for writ of *habeas corpus,* and in which case the court was found to have acted beyond its authority in issuing a writ of mandamus, the United States Supreme Court states as follows:

> "But if the command was in whole or in part beyond the power of the court, the writ, or so much as was in excess of jurisdiction, was void, and the court had no right in law to punish for any contempt of its unauthorized requirements. Such is the settled rule of decision in this court."

Similarly in *Swartz v. United States, supra,* the Court says:

> "It is true that the judgment for contempt as well as the order for injunction, will be set aside on writ of error when the trial court had no jurisdiction to make the order of injunction."

The same rule has been enunciated by the courts of the State of California. In *Maier v. Luce,* 61 Cal. App. 552 at 558, the Court makes the following statement of the rule:

> "No one may be punished for contempt because of his disobedience of a void order."

Exactly the same language was used in *Watchuma Water Company v. Superior Court,* 215 Cal. 734, and the general rule is so stated at 12 *American Jurisprudence,* page 408.

In the case of *Sontag Chain Stores Co., Ltd. v. Superior Court,* 18 Adv. Cal. 65, decided by the Supreme Court of the State of California on May 29, 1941, it was held that the Superior Court may vacate an injunction against picketing when it later appears that the Court acted beyond its jurisdiction in issuing the order due to a misconception of its power. It was argued that this was error only and could not be attacked, but the Court, in distinguishing *United States v. Swift & Co.,* 286 U. S. 106, relied upon by appellant, says that injunctions of the character involved in this case are continuing in character and may be later vacated.

It is interesting to note the following language appearing at page 70:

> "To compel defendant labor unions to seek redress by the indirect method of violation of the terms of the injunction and defense of a contempt proceeding, or certiorari, or *habeas corpus* to secure relief from the contempt commitment, would be to relegate them to a remedy which is indeed circuitous. (See general discussion in 47 Yale Law Journal, pp. 136, *et seq.*)"

The Court obviously recognizes that without question the validity of the injunction order could be attacked in the contempt proceeding. The only question was whether a short cut could be taken by vacating the order. The Court held that it could. This case conclusively determines appellees' right of attack under the California law. Such right, under the Federal law, is similarly conclusively determined by *Beauchamp v. United States, supra.*

It should be noted here that in cases of collateral attack the attack is made by the moving party. In the proceeding at bar, appellant is the moving party, not appellees, thereby bringing the matter again before the Court and recommencing the litigation. The argument of multiplicity of actions does not, therefore, apply, and appellees are entitled to present all defenses.

Moreover, even if the attack could be said to be collateral, which we have shown is not the case, it still can be made inasmuch as the case at bar does not involve error on the part of the referee, but complete lack of

jurisdiction apparent on the face of the record, and, therefore, the ordinary rule that collateral attack will lie upon a void order is applicable. It does not need the citation of authorities to support this rule, which is universally recognized. The only point that can be raised is in its application, and this point is determined by the argument first made in this brief as to the jurisdiction of the referee. It has been shown that the referee was without jurisdiction to make the injunctive order. Such fact is apparent on the face of the record and it is not necessary to go behind the record to determine such fact, although on the state of the present record this can be done. In *Shields v. Shields,* 26 Fed. Sup. 211 (Dist. Ct. Mo.), at page 215, the Court says:

> "This application for *habeas corpus* is a collateral attack on the judgment of the State Court. *Ex parte* Hans Nielsen, 131 U. S. 176, loc. cit. 182, 9 S. Ct. 672, 33 L. Ed. 118. Lack of jurisdiction may be shown in a collateral proceeding. Ruckert v. Moore, 317 Mo. 228, 295 S. W. 794. But in such a proceeding an affirmative finding of a jurisdictional fact may not be contradicted by evidence *aliunde*. Hartzfeld v. Taylor, 207 Mo. 236, 105 S. W. 599; *In re* Lennon, 166 U. S. 548, loc. cit. 553, 17 S. Ct. 658, 41 L. Ed. 1110. Therefore, the residence of petitioner may not be established in this proceeding by parol testimony. But facts appearing upon the face of the record may be utilized to show lack of jurisdiction, and where the record is silent as to a jurisdictional fact the presumption of jurisdiction of a

court of general jurisdiction may be overcome by evidence of facts showing want of such jurisdiction. *In re Mayfield,* 141 U. S. 107, loc. cit. 116, 11 S. Ct. 939, 35 L. Ed. 635."

Under these circumstances the injunction was void and not voidable, and it may be subsequently attacked directly or collaterally.

Much, if not all, of the argument made in the preceding paragraphs in reply to appellant's brief is beside the point, as appellant's argument is beside the point. The authorities reviewed therein show the continuing power of the District Court to vacate or modify its orders. Obviously this includes orders of a referee, a subordinate officer, so long as the bankruptcy case is pending. What the Court did here is tantamount to an implied vacation of the injunctive order. Had the Court, *sua sponte,* seen fit to broaden its order to expressly do what it did impliedly, that is, actually vacate the order, or had application been made by appellees for an order vacating such order, affirmatively acted upon, the vacating by the District Court, in the absence of abuse of discretion, would be conclusive on this appeal. (*Kenyon v. Chain O'Mines* (C. C. A. Colo.), 107 Fed. (2d) 160.

The result is the same in any event, and it is the position of appellees that it was within the continuing jurisdiction of the Court under the circumstances to take the action it did, of dismissal, and that such action, not being an abuse of discretion, or even alleged to be, is not subject to review.

IV.

The Stipulation to the Entry of the Order of Injunction Is Not Grounds for Holding the District Court in Error in Permitting the Attack on Jurisdiction and Dismissing the Contempt.

1. Such Stipulation, Made With Reservation of Objection to the Jurisdiction, Did Not Constitute Grounds for Estoppel.

2. Such Stipulation, So Made, Did Not Constitute a Waiver of, or Consent to Summary Jurisdiction in the Referee.

3. Jurisdiction Cannot Be Conferred by Consent Where No Jurisdiction Exists.

4. Where the Attack Is a Direct and Not a Collateral Attack, Lack of Jurisdiction May Be Shown Even Though Not Apparent on the Face of the Record, and If It Does Not Exist, Consent Cannot Confer It.

Appellant relies on the fact that certain of the appellees stipulated to the issuance of the order of injunction, as grounds for estoppel against the appellees now asserting objections to the jurisdiction. This position is untenable.

In the first place the necessary grounds for estoppel are not present in that there was no reliance, no misleading and no change of position. Appellant had the option in this proceeding of choosing the proper tribunal and the proper legal remedy. It was his choice, and not the choice of appellees that gave rise to the present controversy. He chose injunction as his remedy, and he chose the referee as his tribunal. If he was in error in so doing, that is not the fault of the appellees, and he cannot rely or be misled under these circumstances. The appellees did not choose to go before the referee, but strenuously objected

and maintained their objections to his jurisdiction and that of the Bankruptcy Court at all times, from first to last. [Tr. pp. 29, 30, 92, 94, 96, 150, 154, 156.] They were strangers to the bankruptcy proceeding. They were not trespassing or threatening trespass upon, or damage to the bankrupt's property. They were merely proposing to drill an oil well on their own property. Under these circumstances they were of the view that the referee and the Bankruptcy Court did not have jurisdiction to instruct them as to their method of drilling, and so stated to the referee. [Tr. p. 92.] They reserved at all times their objections to the jurisdiction by appearing specially only [Tr. p. 92], and availing themselves of the right of cross-examination only subject to such objection. [Tr. p. 96.] They did not affirmatively take any part in the proceeding. They did not put on witnesses of their own. The referee, however, overruled their objections to the jurisdiction. Appellees took the position that there was no need to undertake the expense and delay of taking a review, and stipulated to the entry of the order, without conceding the validity of the order. [Tr. p. 156.] In effect they said, "You have dragged us into the Referee's Court. We do not believe that the Referee has any jurisdiction over us so long as we do not actually trespass upon the bankrupt's property, which we have no intention of doing. The order which you are willing to accept, but which we believe is void, is one with which we believe we can comply in any event. No further proceedings are, therefore, necessary at this time, but if we should violate the order we are advising you and the Referee that we do not deem it valid and we are still objecting to the jurisdiction of the Referee and the District Court to enforce it." The appellant obtained what he asked for, which was an order of the referee. It was his option

to obtain a valid order in the proper tribunal and in the proper suit. The appellees were not blowing hot and cold. They were merely saying that if the referee entered a certain order he could do so if he desired, subject to their objection to the fundamental right of the referee to enter it, and that they did not intend to take a review from it. In other words, the appellees were not put to an election. The election was that of the appellant, and he himself suffers the consequences of his own voluntary act in choosing the wrong remedy and the wrong tribunal. Hence, there is no misleading. The record is also devoid of any reference to change of position.

We have shown that there is no estoppel. Further, there is no waiver of any objection to the jurisdiction. Section 23b of the Bankruptcy Act is the only provision of law with which we are familiar, or which has been urged by appellant in this proceeding, under which jurisdiction may be conferred by consent, in the absence of actual jurisdiction over the subject matter. This provision refers, however, solely to cases of adverse possession and has no bearing on the present controversy, which involves only the power of a referee of the United States District Court, either as a court of bankruptcy or a court of equity, or an officer thereof, to enjoin strangers to the bankruptcy proceeding from doing lawful acts on their own property which do not constitute a trespass upon the property of the bankrupt. It is well settled, however, that, even were section 23b applicable, or consent could otherwise constitute a waiver, what the appellees did in this proceeding would not constitute consent to jurisdiction or waiver of their objection to the summary jurisdiction of the referee. A case relied upon by appellant in the District Court was *In re Murray* (C. C. A. 7th), 92 Fed. (2d) 612, which case the District Judge felt to be the

strongest case in appellant's favor. All this case stands for is that objection is made too late when it is not made until after the order has been entered. Even in that case, the Court admits that if objection to jurisdiction is made timely, and such objection is overruled, defendant does not waive such objection by then proceeding with the action. In that case an answer was filed to a summary proceeding to set aside a mortgage and trial was had and an order was made before any objection was made to the jurisdiction. The Court held that while the rule is clear that the referee has no plenary jurisdiction under these circumstances, the defendant may waive the same, and failure to object until the order had been made constituted a waiver.

In *In re Mitchie*, 116 Fed. 749 (District Court, Mass.), the case involved a petition to recover adversely held property. In this case defendant filed an answer and then demurred to jurisdiction. The Court found that the referee had no jurisdiction without the consent of the defendant and that the defendant did not consent. In this connection the Court states that the consent required must be complete and explicit, and cannot be implied. This case was cited with approval *In re Bastanchury Corporation*, decided by the Ninth Circuit Court of Appeals, 62 Fed. (2d) 537. This case arose on an order to show cause directed to the trustee under a bond issue to turn over property. The District Court made a turn over order. The Circuit Court ordered the property returned to the trustee under the bond issue, holding the claim adverse, no consent, and no jurisdiction in the referee. The rule is best emphasized by the decision, *In re Prima* (C. C. A. 7th), 98 Fed. (2d) 952, which involves two defendants, one of whom objected, as appel-

lees objected here, the other of whom did not. After the objection of the first was overruled, answer was filed and the ordinary trial procedure followed. The Appellate Court ruled that, as to the non-objecting defendant, there was a waiver of summary jurisdiction under section 23b of the Act, but as to the other defendant, there was not. To the same effect see *In re Schoenberg* (C. C. A. 2d), 70 Fed. (2d) 321; *In re White Satin Mills,* 25 Fed. (2d) 313 (Dist. Ct., Minn.); *Louisville Trust Co. v. Comingor,* 184 U. S. 18, 22 S. Ct. 293, 46 L. Ed. 413.

The above discussion of cases has been presented merely to show how explicit must be a waiver where even procedural jurisdiction is involved, and apply, as above stated, merely where there is a statutory rule permitting consent to summary jurisdiction, as compared to plenary jurisdiction; in other words, a waiver of a procedural as distinguished from a basically jurisdictional right. The cases cited by the appellant on the point of consent are not in point. In each instance the defendant asked the Court for affirmative relief which is inconsistent with objection to jurisdiction. Appellees here at no time asked for any affirmative relief. The only part they took in the proceeding at all, aside from the objecting to the jurisdiction and cross-examining the appellant's witnesses under the reserved right of objection, was to state, subject to such objection, that they would not take a review from the entry of an order, the form of which they approved, which order the referee had indicated he would make in any event. The cases cited by appellant do not involve anything but the rule, which appellees admit, that a collateral attack may not be made on a judgment which is merely voidable or erroneous. None of them hold that consent is given in the absence of an express intention to give

consent by affirmative action or failure to object, or that consent, when given, cures lack of jurisdiction of the subject matter. An examination of these cases indicates definitely only matters of error or personal jurisdiction where involved, such as defective service. It is also a fact that the case of *Burrough v. Burrough*, 10 Cal. App. (2d) 749, cited by appellant, expressly holds that, if the record shows lack of jurisdiction, it is subject to collateral attack.

In other words, consent may be given to procedural matters, and may cure error, but it cannot supply lack of jurisdiction. Consent to cure procedural matters or error must be explicit. Such consent is not to be found in the record of this case. The District Judge sets forth fully in his opinion his examination of the record in this connection and finds that there was no consent. [Tr. pp. 240 to 252.] Such finding of fact, in any event, is conclusive on this appeal, there being substantial evidence to support it. We, therefore, have a situation whereby the referee has exceeded his jurisdiction both by issuing the injunction after merely a summary hearing, which was not consented to, and assuming jurisdiction to exist in himself, as an officer of the District Court, which even the District Court did not have, and to which appellees did not consent. In this connection it should be noted that even the referee had doubts that he had the right to enter an order as broad in its prohibitions as that entered. Transcript, page 152, where the referee says:

> "I can say right now this Court will not attempt to prevent you from redrilling, but there is a certain course which this Court may prevent you from taking."

And again at page 156 of the transcript, where the referee says:

> "You may review any order this Court makes. I would welcome a review—but if I were going to be reviewed on a question of jurisdiction I would want to give serious consideration to the question."

There is no allegation of diversity of citizenship requisite to the general equity jurisdiction of the District Court. There is also no allegation of lack of an adequate remedy at law. In fact, the record shows the pendency of a civil action to recover damages [Tr. p. 43], brought by the appellant against one of the appellees. The injunction does not enjoin trespass upon or damage to the property of the bankrupt so as to bring the case within the bankruptcy jurisdiction. The injunction enjoins a stranger to the bankruptcy proceeding from doing a lawful act on his own property. It tells him how he shall drill an oil well on his own property. This is far beyond the contemplation of the Congress or the courts as being within the realm of what a referee in bankruptcy can do.

Inasmuch as the referee had no jurisdiction to make the order, even if the holding of the District Court upon the giving of the consent were not conclusive, and even if consent had been given, it could not confer jurisdiction under these circumstances. The rule is too plain to require citation of authority that the jurisdiction of a Court of the United States, as a Federal Court, cannot be waived. *Simpkins' Federal Practice,* 3d Ed., Sec. 30:

> "The jurisdiction of a Court of the United States as a federal court in the strict sense, viz., as regards jurisdictional amount, diversity of citizenship, and

federal question cannot be waived. Nor can the question of jurisdiction of the subject-matter be waived."

Nor can jurisdiction be conferred by consent. *Simpkins' Federal Practice,* 3d Ed., Sec. 31:

"It follows from what has been said in the previous section that federal jurisdiction in the strict sense cannot be conferred by consent."

Similarly as to jurisdiction of the subject-matter, 21 *Corpus Juris Secundum* 127:

"It is not within the power of litigants to invest a court with any jurisdiction or power not conferred on it by law, and accordingly, it is well established as a general rule that, where the court has not jurisdiction of the cause of action or subject-matter involved in a particular case, such jurisdiction cannot be conferred by consent, agreement, or other conduct of the parties. So, also, if the court cannot try the question except under particular conditions or when approached in a particular way, the law withholds jurisdiction unless such conditions exist or unless the court is approached in the manner provided, and consent will not avail to change the provisions of the law in this regard."

Just as the question of method of attack, raised by the appellant, upon examination is determined by the sole question involved in this proceeding—jurisdiction of the referee—so is the question of consent. If the referee had

jurisdiction of the subject-matter of this proceeding, then the injunctive order was valid regardless of consent, and the question of consent or collateral attack is not involved. If the referee did not have jurisdiction to make the order, no consent, even if given, could have rendered the order valid, and such order may be attacked either collaterally or directly.

In addition, even if it could be said that jurisdiction of the subject-matter existed, the appellees were entitled to a plenary suit in the District Court. And no consent was given to summary procedure.

For the foregoing reasons we respectfully submit that the order of the District Court should be affirmed.

Respectfully submitted,

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No. 9790

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE T. GOGGIN, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt,

Appellant,

vs.

BOLSA CHICA OIL CORPORATION, a corporation, THOS. W. SIMMONS, ALLAN A. ANDERSON, WILLIAM H. CREE, H. H. McVICAR, C. M. ROOD, and M. M. McCALLEN CORPORATION, a corporation,

Appellees.

APPELLANT'S OPENING BRIEF.

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APPELLANT'S OPENING BRIEF.

Jurisdiction.

This is an appeal from a decision of the United States District Court, Southern District of California, Central Division, rendered February 7, 1941, wherein and whereby the District Court dismissed the certificate of contempt of the Referee [Tr. pp. 83-85]. Notice of appeal was given within thirty days from February 7, 1941, to-wit: February 13, 1941 [Tr. pp. 86-87]. Section 24-A of the Bankruptcy Act of 1938 vests the Circuit Court with jurisdiction over such appeal.

The District Court was vested with jurisdiction by virture of Sections 2(15) and 41 of the Bankruptcy Act of 1938.

Statement of the Case.

On April 20, 1940, an order to show cause was issued by the Referee in Bankruptcy [Tr. pp. 27-28], requiring the appellee, Bolsa Chica Oil Corporation, to appear and show cause why such appropriate order should not be made to protect the "Huntington Shore" well, being an asset of the bankrupt estate of Jack Dave Sterling, Bankrupt, from damage resulting from the redrilling of the "Petroleum Well" owned by the appellee, Bolsa Chica Oil Corporation. Said order to show cause was served, together with a copy of the petition of the Trustee and copies of the affidavits of Vernon L. King, petroleum engineer, and Jack Dave Sterling, the bankrupt [Tr. pp. 19-27], upon which said order to show cause was based.

Thereupon a hearing was had before the Referee, pursuant to said order to show cause, at which the Bolsa Chica Oil Corporation appeared by its attorneys, and after hearings on April 26, 1940 and on May 1, 1940, an order was made by the Referee on May 15, 1940 [Tr. pp. 29-32] which order, among other things, enjoined the appellee, Bolsa Chica Oil Corporation, its agents and employees, from redrilling its "Petroleum Well" in such a manner as would cause it to come closer than two hundred (200) feet from the "Huntington Shore" well at any horizontal plane at a point below the depth of 3800 feet below sea level also, that the circulating fluid used in drilling said "Petroleum Well" should be virgin crude oil, and that no cementing operations be conducted without the written consent of appellant; that said order of injunction was approved by the appellee, Bolsa Chica Oil Corporation [Tr. p. 32]; that said order of injunction was stipulated to in open court by the appellee, Bolsa Chica Oil Corporation

[Tr. p. 152, fol. 189; p. 153, fol. 190, pp. 155, 156, 172]; that in said written order of injunction, while appellee, Bolsa Chica Oil Corporation, acknowledged that it was stipulating thereto, and approved the contents thereof, it caused to be inserted a reservation of objection to the general jurisdiction of the Bankruptcy Court.

That thereafter a petition to have the Bolsa Chica Oil Corporation, *et al.,* certified for contempt was filed by appellant with the Referee on August 22, 1940, and an order to show cause issued thereon, directed to Bolsa Chica Oil Corporation, McVicar-Rood, Inc., a corporation, M. M. McCullum Corporation, a corporation, H. H. McVicar, C. M. Rood, M. M. McCullum, Thomas W. Simmons, "John Doe" Anderson, and William H. Cree and Warren S. Pallette [Tr. pp. 33-39], to show cause why they should not be certified for contempt for violating or aiding and abetting in the violation of the order of injunction issued May 15, 1940.

That pursuant to said order to show cause hearings were had before the Referee on August 30, 1940, September 26, 1940 and October 1, 1940, as a result of which the Referee made a certificate of contempt containing findings of fact and conclusions of law, based upon which the Referee certified the Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, M. M. McCallen Corporation, H. H. McVicar, C. M. Rood and William H. Cree to the United States District Court as being in contempt for violating the injunction of May 15, 1940, and for such further proceedings as might be proper before

the District Court [Tr. pp. 53-72]; that an order to show cause was issued by the Referee on January 13, 1941, requiring the Bolsa Chica Oil Corporation, Thomas W. Simmons, Allen A. Anderson, M. M. McCallen Corporation, H. H. McVicar, C. M. Rood and William H. Cree to appear and show cause why they should not be adjudged in contempt pursuant to the certificate of the Referee [Tr. pp. 80-81]; that a motion in writing was filed by the Bolsa Chica Oil Corporation, Thos. W. Simmons and Allen A. Anderson, together with affidavits of W. S. Pallette and Donald H. Ford, upon which an order to show cause was issued why the certificate of contempt of the Referee should not be dismissed [Tr. pp. 73-79].

That thereafter the order to show cause of the Referee, based on the certificate of the Referee for contempt, and the order to show cause of the appellees, Bolsa Chica Oil Corporation, Thos. W. Simmons and Allen A. Anderson, came on for hearing on January 20, January 27, and January 30, 1941, before the Honorable Leon R. Yankwich, on which dates the matter was argued without evidence of any kind being received, and on February 7, 1941, said District Judge made an order sustaining the objection of the appellees to the jurisdiction of the Referee to issue such certificate of contempt, and sustaining the collateral attack of appellees that the Referee had no jurisdiction to make the order of injunction of May 15, 1940, the basis of such certificate of contempt; and made its further order dismissing the Referee's certificate of contempt [Tr. pp. 83-85].

Statement of the History of the Case.

The certificate of contempt of the Referee, found on pages 53-72 of the transcript, succinctly states the background leading up to the issuance of the injunction of May 15, 1940, the violation of the injunction, hearing on the order to show cause why the appellees should not be certified in contempt, and the issuance of the certificate after such hearing. Such background, as so disclosed by the certificate, is as follows:

That appellant owns an oil well known as the "Huntington Shore Well", located in what is known as the Huntington Beach oil field, and operated under an easement granted by the state of California, being easement Number 309; that said well constitutes one of the principal assets of the bankrupt estate of the appellant; that on or about September 20, 1936, the Termo Oil Company, being the holder of a similar easement to that of the appellant in said Huntington Beach oil field, commenced the re-drilling of its "Termo Well", and as a result of said re-drilling, mud, together with sand, cement, and other foreign substances were forced through the oil sands from the "Termo Well" into the "Huntington Shore Well", causing the equipment in the "Huntington Shore Well" to become stuck, and making it impossible to operate or produce said "Huntington Shore Well" [Tr. p. 55]; that as a result, appellant expended, on what is known as a "fishing job" the sum of approximately $20,000.00 without being able to free such equipment that was clogged and stuck by reason of such operations of the Termo Oil Company; that thereafter it became necessary for appellant to redrill said "Huntington Shore Well" at a cost of $80,000.00, plus a surrender of a twenty per cent interest (20%) in said well, in addi-

tion thereto; that said "Huntington Shore Well", after being redrilled was again placed on production on August 22, 1937, with an average daily production of about 295 barrels; that about April 15, 1940, appellee, Bolsa Chica Oil Corporation, commenced the redrilling of its well, known as "Petroleum Well", which likewise was operated under an easement from the state of California in the Huntington Beach oil field; that on said date appellee, Bolsa Chica Oil Corporation, was familiar with and was aware of the damaging effect of the drilling of the "Termo Well" on the "Huntington Shore Well" [Tr. p. 56]; that an application was made to enjoin appellee, Bolsa Chica Oil Corporation, from drilling its "Petroleum Well" closer than 200 feet from the "Huntington Shore Well", and from using mud as a circulating fluid in the redrilling of said well; that the testimony showed that if said well was drilled closer than 200 feet from the "Huntington Shore Well", and if mud was used, that the mud would be carried through the oil sands into the "Huntington Shore Well" and would irreparably injure and damage said well; that thereupon, and pursuant to the stipulation of the attorneys for appellees, Bolsa Chica Oil Corporation, and attorneys for appellant, made in open court, an injunction was made by the Referee enjoining the appellee, Bolsa Chica Oil Corporation, from coming closer than two hundred feet from the "Huntington Shore Well", and from using mud as a circulating fluid in the redrilling of its "Petroleum Well" [Tr. p. 57]; that said injunction was issued on May 15, 1940, same being approved by the appellee, Bolsa Chica Oil Corporation; that written notice of the entry of said injunction, together with a copy of the order of injunction, was served upon both the appellee, Bolsa Chica Oil Corporation, and its attorneys of record,

on May 17, 1940, [Tr. pp. 58-59]; that no petition for review or appeal was taken from said injunction, and that said injunction has become final and absolute by operation of law [Tr. p. 58].

That after the granting of said injunction and with full knowledge thereof, appellee, Bolsa Chica Oil Corporation, resumed the redrilling of said "Petroleum Well", by using mud as a circulating fluid in direct violation of said injunction [Tr. p. 59]; that as a result of the use of mud as a circulating fluid in the redrilling of said well, mud in liquid form, carrying with it sand and other foreign substances, infiltrated through the oil sands and was forced up into the said "Huntington Shore Well" forming a column of mud in said well of 3700 feet from the bottom of said well; that as a result thereof, production from said "Huntington Shore Well" ceased and said "Huntington Shore Well" was off production for a period of twenty days during which operations were carried on by appellant to clean out and dislodge such mud, sand and other foreign substances [Tr. p. 60]; that specimens of the mud lost in the redrilling of said "Petroleum Well" were tested, analyzed and examined, and shown conclusively to be the mud used by the appellee, Bolsa Chica Oil Corporation, in said redrilling; that at the time of the commencement of said redrilling operations, said "Huntington Shore Well" was producing 260 barrels of oil per day; that as a result of such mud being forced into said well, by reason of such operations on the redrilling of the "Petroleum Well", appellant lost production for twenty days, and the

production of the well was permanently reduced to 160 barrels of oil per day [Tr. p. 61]; that as a result of the use of mud as a circulating fluid in said "Petroleum Well", the production of the "Huntington Shore Well" has been reduced to the extent of approximately sixty (60) barrels of oil per day for the life of said well [Tr. p. 62]; that mud was used by appellee, Bolsa Chica Oil Corporation, with the knowledge and at the instance and direction of Thomas W. Simmons, its president, and Allen A. Anderson, its superintendent; that the damage so sustained by appellant was anticipated by appellant in applying for said injunction and the purpose of issuing such injunction was to avoid such damage to the property of appellant; that the appellee, Bolsa Chica Oil Corporation, knew such consequence and damage would result from the use of mud as a circulating fluid in the redrilling of its "Petroleum Well"; that after said mud, in liquid form, had infiltrated through the oil sands from the "Petroleum Well" to the "Huntington Shore Well", appellee, Bolsa Chica Oil Corporation, suspended drilling of its "Petroleum Well" on or about June 10, 1940 [Tr. p. 63]; that information having come to the appellant that appellee, Bolsa Chica Oil Corporation, was about to resume redrilling of said well by the use of mud as a circulating fluid, a letter was addressed to said appellee, Bolsa Chica Oil Corporation on July 31, 1940, calling its attention to the injunction of the Court against the use of mud, and enclosing a copy of said injunction; that thereafter (and on August 1, 1940) a conference was

had between appellees, Thomas W. Simmons, president of Bolsa Chica Oil Corporation, Warren S. Pallette and Wililam H. Cree, attorneys for said Bolsa Chica Oil Corporation, Allen A. Anderson, drilling superintendent of Bolsa Chica Oil Corporation, and Vernon L. King, petroleum engineer for the Trustee in Bankruptcy, R. D. Holdredge, representing the Trustee, and Joseph J. Rifkind, one of the attorneys for the Trustee. At said conference appellees aforesaid sought to secure an agreement to eliminate from said injunction the provision against the use of mud as a circulating fluid [Tr. p. 64]; that at said conference appellees' attention was called to the fact that the use of mud in the "Petroleum Well" theretofore had caused a column of mud 3700 feet high to rise in the "Huntington Shore Well" and that such fact was the best evidence that the use of mud as a circulating fluid would damage the "Huntington Shore Well" and that no modification of the injunction would be stipulated to; that said Thomas W. Simmons stated at said conference that a large amount of money had been spent by his company and some way would have to be found to resume drilling operations despite the injunction; that said William H. Cree, one of the attorneys for appellee, Bolsa Chica Oil Corporation, advised that said injunction be ignored [Tr. p. 65]; that counsel for appellant stated that the injunction was in full force and effect and that if mud was used, contempt proceedings would be instituted; that previous to this conference, a conference was had between said Thomas W. Simmons and Raphael Dechter, also of

counsel for appellant, wherein a modification of said injunction as to the provision against the use of mud was sought and was refused [Tr. p. 66]; that thereafter appellant received information that some arrangement had been effected between the Bolsa Chica Oil Corporation and its agents, officers and employees and H. H. McVicar, C. M. Rood and M. M. McCallen Corporation, the other appellees, whereby drilling operations were being resumed in the "Petroleum Well"; that a letter was then sent by appellant to McVicar-Rood, Inc. under date of August 21, 1940, advising them of the injunction and the restriction against the use of mud in the redrilling of said "Petroleum Well" [Tr. p. 67]; that the appellees entered into a conspiracy for the purpose of violating said injunction, and in order to give color to said transaction, entered into an agreement and an assignment, and in disregard of said injunction and the letters from appellant, commenced redrilling said well with the use of mud as a circulating fluid on or about August 22, 1940; that thereupon appellant filed a petition to certify said appellees for contempt, and said appellees, even after the service upon them of said petition, continued to use mud as a circulating fluid in the redrilling of said "Petroleum Well" [Tr. pp. 68-69]. From such facts, the Referee concluded that said appellees were in contempt of Court for violating said injunction and for aiding and abetting in the violation thereof, and in accordance with the procedure prescribed in section 41 of the Bankruptcy Act, duly certified the appellees to the District Court for contempt.

Questions Involved in This Appeal.

1. Where an order of injunction has been made by a Referee in Bankruptcy, no review or appeal having been taken therefrom within the time and in the manner provided by law, can said order be collaterally attacked as being in excess of the jurisdiction of the bankruptcy court?

2. Where the Referee, pursuant to section 41 of the Bankruptcy Act, certifies for contempt the appellees, for having violated a previous order of injunction which had become final, may the District Judge permit a collateral attack on the order of injunction, declare such order of injunction void, and dismiss the Referee's certificate of contempt based upon the violation of such order of injunction?

3. Where the appellee, Bolsa Chica Oil Corporation, has stipulated and consented to the making of an order of injunction, and has stated that no review would be taken from such order and that such order would be binding upon it, may said appellee, after such stipulated order has become final, question the jurisdiction of the bankruptcy court to make such order of injunction, when certified for contempt in violation of the terms of such consent or stipulated order?

4. Where the appellee, Bolsa Chica Oil Corporation, has stipulated to an order of injunction and has stated that no review will be taken therefrom and that it will be bound thereby, is not said appellee estopped from questioning the jurisdiction of the

bankruptcy court to make such order of injunction, at a subsequent hearing on an order to show cause why it should not be certified for contempt for violating the provisions of such consent order of injunction?

5. Does not the Bankruptcy Court have jurisdiction, both as a court of equity, and under the provisions of the Bankruptcy Act, to enjoin any interference or threatened interference with property in the custody of the bankruptcy court?

6. Does not the Bankrutcy Court have the power to adjudge appellee, Bolsa Chica Oil Corporation, in contempt for interfering with the property of the bankrupt estate, particularly so where such appellee had previous notice that the doing of an act in a certain manner would interfere with the property of the bankrupt estate, and where such appellee had agreed in writing not to do certain acts, the result of which would naturally cause damage to the property of the bankrupt estate, and where such appellee, contrary to its agreement, wilfully commits such acts, as a natural result of which the property of the bankrupt estate is damaged and the administration of the bankrupt estate interfered with.

Points Upon Which Appellant Relies.

The statement of the points upon which appellant will rely in this appeal is to be found at pages 267-269 of the transcript. These points are numbered and appear preceding the arguments addressed thereunder in this brief.

ARGUMENT.

I.

The District Court Erred in Permitting a Collateral Attack to Be Made Upon the Jurisdiction of the Referee to Render the Injunction (the Violation of Which Was the Basis of the Referee's Certificate of Contempt), Said Injunction Having Become Final, and No Appeal or Other Manner of Review Permitted by Law Having Been Taken Therefrom.

POINT 1. The District Court erred in rendering the order dismissing the Referee in Bankruptcy's Certificate of Contempt.

POINT 2. The District Court erred in sustaining objections to the jurisdiction of the District Court to hear the matter arising under the Referee's Certificate of Contempt.

POINT 3. The District Court erred in permitting a collateral attack to be made upon the jurisdiction of the Referee to render the injunction (the violation of which was the basis of the Referee's Certificate of Contempt), said injunction having become final, and no appeal or other manner of review permitted by law having been taken therefrom.

The order of injunction was made by the Referee on May 15, 1940. Said order was stipulated to in open court. In this connection, we quote from the findings of the Referee embodied in the certificate of contempt, at pages 57-58 of the transcript as follows:

> "That after the testimony introduced on behalf of the trustee in bankruptcy and upon the conclusion of the cross-examination by the attorneys for the Bolsa Chica Oil Corporation of the witnesses called on behalf of the trustee in bankruptcy, the attorneys for

the Bolsa Chica Oil Corporation stipulated in open court to the granting of an injunction against the Bolsa Chica Oil Corporation restraining them from coming closer than 200 feet from the Huntington Shore Well and prohibiting the Bolsa Chica Oil Corporation from using mud as a circulating fluid in the redrilling of this well. That pursuant to the stipulation entered into between the attorneys for the trustee in bankruptcy and the attorneys for the Bolsa Chica Oil Corporation an injunction was submitted to the above entitled court which had been previously approved as to form and content by the attorneys for the trustee in bankruptcy and the attorneys for the Bolsa Chica Oil Corporation, and said injunction was issued by the court on May 15, 1940."

After the Trustee had introduced evidence, both oral and written, in support of the order to show cause why an appropriate order should not be made by the Referee to protect the property of the bankrupt estate, the following took place, as shown by pages 150-160 of the transcript:

"Mr. Dechter: That is all for the petitioner, for the Trustee.

Mr. Borden: I think I made the statement in the first instance that our cross-examination was not to be construed as any waiver of our objection to the jurisdiction.

The Referee: Oh yes.

Mr. Borden: I don't think there is any question about that. We have no evidence to offer at the present time. I might have if there is any question in Your Honor's mind whether or not the Court, in a summary proceeding of this kind against a total stranger, and under these circumstances, has a right to take any action or to restrain us from proceeding.

I should like to have a continuance in order to put on some testimony without conceding the jurisdiction of the Court. I think the Court is entitled to have the benefit, no matter what order it makes with respect to directing the Trustee to commence plenary action or any other remedy available to him, of hearing testimony on both sides.

Mr. Dechter: We have no objection to giving Mr. Borden [188] a reasonable length of time.

The Referee: From what I know about this case here is the way I feel now: I don't think the bankruptcy court has any jurisdiction to tell a stranger where or how he should drill his well so long as that stranger does not interfere or trespass upon the rights of the bankrupt. Up to that point this Court has not anything to say. If there is a danger of trespassing or damaging the bankrupt's property, I think then the Court would have jurisdiction, that is, covering that particular phase of it. That is my offhand impression.

Mr. Borden: Well, I think there is no doubt if we were actually trespassing upon the property of the bankrupt, there is no doubt in my mind but what the Court would have ample opportunity to restrain us, but here we are drilling in separate lots where there is no interference at all. We are doing the same thing they have done since the matter has been in bankruptcy, Your Honor. They have drilled within one hundred feet of us, according to the testimony before the Court, but now they seek to enjoin us from proceeding to do the very same thing, to re-drill and place our well on production.

The Referee: I can say right now this court will not attempt to prevent you from re-drilling, but there is a certain course which this Court may prevent you from taking.

Mr. Pallette: I think we can stipulate to an order, if [189] you want to make one, restraining us from coming within a certain distance.

Mr. Dechter: That is agreeable.

The Referee: What would be a reasonable distance, the regulation of the Department?

Mr. Dechter: I am willing to make it within the radius of one hundred feet, or the diameter of two hundred feet. In other words, if counsel will agree—

The Referee: Why not follow the regulation—

Mr. Dechter: That is agreeable.

The Referee: —as Exhibit 1 provides?

Mr. Dechter: I might also call the Court's attention to the Huntington Townsite agreement which is binding on the Bolsa Chica Corporation, which contains this provision:

'Said member, with reference to said well, shall comply with all of the laws of the State of California and all rules and regulations of any agency of the State of California having jurisdiction thereof.' Now, other members of this association have agreed to comply with those rules and this agency has jurisdiction.

Mr. Borden: That is not before this Court. It is a matter of whether or not we were *interfering* with the bankrupt's property.

Mr. Rifkind: I understand it is agreeable that an injunction be granted embodying the regulations—

Mr. Pallette: No. [190]

Mr. Rifkind: What is that?

Mr. Pallette: No.

Mr. Rifkind: What do you suggest?

Mr. Pallette: I suggested we would be willing to stipulate that an injunction be granted restraining us from coming within a reasonable distance of the well.

Mr. Dechter: All right.

Mr. Pallette: I think we will have to consult with our engineers as to what they deem to be a reasonable distance.

Mr. Dechter: If you make it one hundred feet it will end the matter.

The Referee: Is it one hundred or two hundred?

Mr. Dechter: Within a radius of one hundred feet or a diameter of two hundred feet.

Mr. Borden: No one ever contended we would get any closer than that.

The Referee: Suppose, gentlemen, I continue this matter and then you can see if you can get together on an order?

Mr. Pallette: I wouldn't be surprised but what we could stipulate on one hundred feet, but I don't think I am justified in doing so without consulting our engineers.

Mr. Borden: I think that is a good idea. Let the record show, if Your Honor please, that by suggesting that we are willing to submit to the jurisdiction of the Court, that we do not do so until we actually do so.

The Referee: Yes, I understand that. Suppose I continue [191] this matter for a week or ten days.

Mr. Pallette: Could it be continued for a shorter time than that. We have a hearing set before the

State Lands Commission some time during the middle of next week *at which time we hope to get the consent of the State to proceed.*

The Referee: You are not going to proceed until you do that?

Mr. Pallette: We are closed down. We have been closed down for about a week, and we have no intention of proceeding now. We hope to work out an agreement with the Chairman of the State Lands Commission some time during the week. I suggest a continuance be granted until Tuesday or Wednesday.

The Referee: Of this next week?

Mr. Pallette: Yes.

Mr. Dechter: Of the coming week, or the week following?

Mr. Pallette: Next Tuesday or next Wednesday.

Mr. Borden: I don't think it would take any time at all.

Mr. Dechter: I suggest we make it Wednesday, Your Honor.

The Referee: Well, due to the condition of my calender I will continue it until May 1st, in the afternoon, 2:00 p. m.

Mr. Rifkind: Do I understand that until that time there will be no resumption of drilling?

Mr. Pallette: That is correct, we will consent to not re-drill before next Wednesday, that is, to make any holes.

The Referee: Very well.

(Whereupon an adjournment was taken to the hour of 2:00 p. m., May 1st, 1940.) [192]

Los Angeles, California. Wednesday, May 1, 1940. 2:00 o'clock p. m. Session.

* * * * * * * *

The Referee: Have you accomplished anything in the matter of Jack Dave Sterling?

Mr. Rifkind: Yes, Your Honor. We have reached a stipulation that an injunction may be issued by the Court against the Bolsa Chica Oil Corporation. We have already given the specific language to the reporter and I would like him at this time to read it to the Court.

The Referee: Is the stipulation generally agreed to between counsel?

Mr. Borden: Yes.

The Referee: You may state generally what it is.

Mr. Borden: We have stipulated as to the order. We do not concede jurisdiction of the Court. We are going to agree that we will not review the order of Court and will be bound by the order. However, I make that statement because we do not want to *generally* concede jurisdiction.

The Referee: You may review any order this Court makes I would welcome a review—but if I were going to be reviewed on a question of jurisdiction I would want to give serious consideration to the question.

Mr. Borden: I will say you will not be required to do so; but we do not want to submit to any proceedings in a [193] court where we are strangers.

Mr. Rifkind: I would like to have the reporter read aloud our stipulation.

The Referee: Very well.

Mr. Borden: I agree with you, but I wanted our position made perfectly clear.

(Whereupon the stipulation referred to was read by the reporter, as follows:)

'Bolsa Chica Oil Corporation, its superintendent, agents and employees, shall be restrained and enjoined from drilling, re-drilling or sidetracking its Petroleum Well, also known as Fee No. 1 Well at Huntington Beach, California, so that it comes closer than 200 feet from the Huntington Shore Well measured on a horizontal plane at any point below the depth of 3800 feet below sea level as the course of the Huntington Shore Well is shown on the plat or chart marked Trustee's Exhibit 5.

In determining whether such drilled, re-drilled or sidetracked portion of Petroleum Well, also known as Fee No. 1 Well approaches within 200 feet of the Huntington Shore Well, measured as above set forth, the course of the Huntington Shore Well in said plat shall be as delineated on said plat and shall be conclusive as to the parties; and the distance therefrom shall be conclusively determined by plotting the course of the drilled, re-drilled or sidetracked portion of said [194] Fee No. 1 Well on said plat, based upon single shot surveys taken during the course of the drilling, redrilling or sidetracking of the Petroleum Well, also known as Fee No. 1 Well, at approximately every 100 feet, which single shot surveys shall be made available to the Trustee in Bankruptcy or his representatives as the same are from time to time taken and made;

That the circulating fluid in drilling, re-drilling, or sidetracking of said Petroleum Well, also known as Fee No. 1 Well, shall be virgin crude oil maintained at a grade and gravity consistent with good oil practice in said field, and that no mud or other foreign substances of any kind shall be used in lieu

of such circulating fluid, provided that a substitute circulating fluid may be used as may be mutually agreed to in writing between the petroleum engineers for the respective parties thereto.'

* * * * * * * *

The Referee: Is that stipulation agreeable, gentlemen?

Mr. Borden: Yes.

Mr. Rifkind: We will prepare an order.

The Referee: Very well, prepare a formal order.

Mr. Rifkind: It will be approved as to form and contents by both sides.

Now, I want to introduce as Trustee's exhibit next in order this plat showing among other things the course of the [197] Huntington Shore Well and the course of the old Bolsa Chica Well.

Mr. Pallette: The present course.

Mr. Rifkind: The present course of the Bolsa Chica Well, known as Petroleum Well, and also known as Fee No. 1 Well.

The Referee: The plat will be marked Trustee's Exhibit No. 5.

(The document referred to is marked Trustee's Exhibit No. 5, in evidence.)"

It is the contention of the appellant that even had not said order of injunction been stipulated to, and even had the order been in excess of the jurisdiction of the Bankruptcy Court, jurisdiction is an issue, like any other issue in a case, which, after an order becomes final, is not subject to any reopening or further hearing thereon. A decision which is *res judicata* concludes all issues raised thereunder, and that could have been raised thereunder.

In this case one of the issues raised by appellees was the question of the jurisdiction of the Bankruptcy Court. Thus, once having raised such question, appellees are now finally bound by the decision of the Bankruptcy Court in disposing of such issue, and are forever concluded from making a collateral attack thereon.

This point has been definitely decided by the United States Supreme Court in the following decisions:

In the case of *Baldwin v. Iowa State Traveling Men's Ass'n.*, 283 U. S. 522, 51 S. Ct. 517, 75 L. Ed. 1244, involving an action brought against defendant in the United States District Court of Missouri, defendant having appeared specially for the purpose of objecting to the jurisdiction of the Court. The Court overruled the objection and the defendant took no further steps of any kind in the proceeding after the Court overruled the objection. Judgment, was rendered against defendant in said proceeding. Later on the judgment creditor in said suit brought an action at the residence of the defendant, which was in the United States District Court of Iowa. Defendant claimed that the Missouri District Court had no jurisdiction to render the judgment. The Iowa District Court sustained this defense and dismissed the action. The question of whether such a collateral attack could be made on the first judgment was taken to the United States Supreme Court, which Court, in a decision by Justice Roberts, makes the following statement (283 U. S. pp. 524, 525, 526):

> "The substantial matter for determination is whether the judgment amounts to *res judicata* on the question of the jurisdiction of the court which rendered it over the person of the respondent. *It is of*

no moment that the appearance was a special one expressly saving any submission to such jurisdiction. That fact would be important upon appeal from the judgment, and would save the question of the propriety of the court's decision on the matter even though after the motion had been overruled, the respondent had proceeded, subject to a reserved objection and exception, to a trial on the merits. * * * *The special appearance gives point to the fact that the respondent entered the Missouri court for the very purpose of litigating the question of jurisdiction over its person. It had the election not to appear at all. If, in the absence of appearance, the court had proceeded to judgment and the present suit had been brought thereon, respondent could have raised and tried out the issue in the present action, because it would never have had its day in court with respect to jurisdiction.* * * * It had also the right to appeal from the decision of the Missouri district court, as is shown by *Harkness v. Hyde,* 98 U. S. 476, 25 L. ed. 237, *supra,* and the other authorities cited. It elected to follow neither of those courses, but, after having been defeated upon full hearing in its contention as to jurisdiction, it took no further steps, and the judgment in question resulted.

"Public policy dictates that there be an end of litigation; that those who have contested an issue shall be bound by the result of the contest, and that matters once tried shall be considered forever settled as between the parties. We see no reason why this doctrine should not apply in every case where one voluntarily appears, presents his case and is fully heard, and why he should not, in the absence of fraud, be thereafter concluded by the judgment of the tribunal to which he has submitted his cause." (Italics ours.)

Another of such Supreme Court decisions is *Chicot County Drainage Dist. v. Baxter State Bank,* 308 U. S. 371, 60 S. Ct. 317, 84 L. Ed. 329 (rehearing denied 309 U. S. 695, 60 S. Ct. 581, 84 L. Ed. 1035) which involved a bankruptcy proceeding under the municipal reorganization and adjustment provision for the adjustment of bonds of the drainage district. In this case it appeared that the particular bondholder had been a claimant in the reorganization proceedings. Notwithstanding such reorganization, and notwithstanding the fact that a claim had been filed, the bondholder filed suit on its original bonds, contending that the bankruptcy court in the reorganization proceeding was without jurisdiction, for the reason that the Municipal Reorganization Act was ruled unconstitutional by the United States Supreme Court. Chief Justice Hughes, in writing the opinion, states as follows at 308 U. S. at pp. 374, 375:

> "The courts below have proceeded on the theory that the Act of Congress, having been found to be unconstitutional, was not a law; that it was inoperative, conferring no rights and imposing no duties, and hence affording no basis for the alleged decree. *Norton v. Shelby County,* 118 U. S. 425, 442; *Chicago, I. & L. Ry. Co. v. Hackett,* 228 U. S. 559, 566. It is quite clear, however, that such broad statements as to the effect of a determination of unconstitutionality must be taken with qualifications. The actual existence of a statute, prior to such a determination, is an operative fact and may have consequences which cannot justly be ignored. The past cannot always be erased by a new judicial declaration. The effect of the subsequent ruling as to invalidity may have to be considered in various aspects,—with respect to

particular relations, individual and corporate, and particular conduct, private and official. Questions of rights claimed to have become vested, of status, of prior determinations deemed to have finality and acted upon accordingly, of public policy in the light of the nature both of the statute and of its previous application, demand examination. Those questions are among the most difficult of those which have engaged the attention of courts, state and federal, and it is manifest from numerous decisions that an all-inclusive statement of a principle of absolute retroactive invalidity cannot be justified. Without attempting to review the different classes of cases in which the consequences of a ruling against validity have been determined in relation to the particular circumstances of past transactions, we appropriately confine our consideration to the question of *res judicata* as it now comes before us."

Also quoting from the syllabus, as follows:

"The lower federal courts, including the District Court sitting as a court of bankruptcy, though their jurisdiction is limited to that prescribed by Acts of Congress, are nevertheless courts with authority, when parties are brought before them in accordance with the requirements of due process, to determine whether or not they have jurisdiction to entertain the cause and for this purpose to construe and apply the statute under which they are asked to act. *Their determinations of such questions, while open to direct review, may not be assailed collaterally.*"

And at page 376 the court said:

"The argument is pressed that the District Court was sitting as a court of bankruptcy, with the limited jurisdiction conferred by statute, and that, as the statute was later declared to be invalid, the District Court was without jurisdiction to entertain the proceeding and hence its decree is open to collateral attack. We think the argument untenable. The lower federal courts are all courts of limited jurisdiction, that is, with only the jurisdiction which Congress has prescribed. *But none the less they are courts with authority, when parties are brought before them in accordance with the requirements of due process, to determine whether or not they have jurisdiction to entertain the cause and for this purpose to construe and apply the statute under which they are asked to act. Their determinations of such questions, while open to direct review, may not be assailed collaterally.*"

Also, at page 378, where it was said:

"The remaining question is simply whether respondents having failed to raise the question in the proceeding to which they were parties and in which they could have raised it and had it finally determined, were privileged to remain quiet and raise it in a subsequent suit. *Such a view is contrary to the well-settled principle that res judicata may be pleaded as a bar, not only as respects matters actually presented to sustain or defeat the right asserted in the earlier proceeding, 'but also as respects any other available matter which might have been presented to that end.' Grubb v. Public Utilities Commission,* 281 U. S. 470, 74 L. Ed. 972, 50 S. Ct. 374, *supra; Cromwell v. Sac. County,* 94 U. S. 351, 24 L. Ed. 195, *supra.*"

(Italics are those of appellants wherever they appear.)

Another United States Supreme Court case directly in point is *Stoll v. Gottlieb,* 305 U. S. 165, 59 S. Ct. 134, 83 L. Ed. 104 (rehearing denied 305 U. S. 675, 59 S. Ct. 250, 83 L. Ed. 437), which involves a question arising out of a proceeding under section 77-B of the Bankruptcy Act. In said case the plaintiff had not filed a claim in the original 77-B proceeding wherein an order of reorganization had been made. However, after the order approving the plan of reorganization had been made, he filed a petition to vacate the same insofar as it eliminated the liability of Stoll as a guarantor under the bonds held by him. This petition to vacate was denied. Thereafter the bondholder filed a suit in the Municipal Court of Chicago for the full amount of his bonds, and contended that the decree of the bankruptcy court was void for lack of jurisdiction. The Municipal Court of Chicago held with the bondholder and awarded him judgment against Stoll for the full amount of the bonds, and disregarded the plan of reorganization approved by the United States District Court. An appeal was taken to the Appellate Court of Illinois, which reversed the Municipal Court; then an appeal was taken to the Supreme Court of Illinois which reversed the intermediate appellate court and upheld the Municipal Court judgment. Thereupon a review was taken to the United States Supreme Court which in turn reversed the Supreme Court of Illinois and held that when the bondholder filed his petition to vacate the decree of the District Court he subjected himself to the jurisdiction of said court for all purposes, both as to subject-matter and as to person.

We quote from the language of the opinion by Justice Reed at 305 U. S., pp. 171, 172, as follows:

> "The inquiry is to be directed at the conclusiveness of the order releasing the guarantor from his obligation *assuming the Bankruptcy Court did not have jurisdiction of the subject matter of the order, the release in reorganization of a guarantor from his guaranty of the debtor's obligations.*
>
> "A court does not have the power, by judicial fiat, to extend its jurisdiction over matters beyond the scope of the authority granted to it by its creators. There must be admitted, however, a power to interpret the language of the jurisdictional instrument and its application to an issue before the court. Where adversary parties appear, a court must have the power to determine whether or not it has jurisdiction of the person of a litigant, or whether its geographical jurisdiction covers the place of the occurrence under consideration. *Every court* in rendering a judgment tacitly, if not expressly, *determines its jurisdiction over the parties and the subject matter. An erroneous affirmative conclusion as to the jurisdiction does not in any proper sense enlarge the jurisdiction of the court until passed upon by the court of last resort, and even then the jurisdiction becomes enlarged only from the necessity of having a judicial determination of the jurisdiction over the subject matter.* When an erroneous judgment, whether from the court of first instance, or from the court of final resort, is pleaded in another court or another jurisdiction the question is whether the former judgment is *res judicata.* After a federal court has decided the question of the jurisdiction over the parties as a contested issue, *the court in which the plea of res judi-*

> *cata is made has not the power to inquire again into that jurisdictional fact.* We see no reason why a court, in the absence of an allegation of fraud in obtaining the judgment, should examine again the question whether the court making the earlier determination on an actual contest over jurisdiction between the parties, *did have jurisdiction of the subject matter of the litigation.* In this case the order upon the petition to vacate the confirmation settled the contest over jurisdiction." (Italics ours.)

In this case of *Stoll v. Gottlieb, supra,* it was urged by the respondent there, as it is urged by the appellees in the present case, that the order was a complete nullity and subject to collateral attack. Such contention in the briefs of respondent there were answered by the following language in the decision, at page 172:

> "Courts to determine the rights of parties are an integral part of our system of government. *It is just as important that there should be a place to end as that there should be a place to begin litigation. After a party has his day in court, with opportunity to present his evidence and his view of the law, a collateral attack upon the decision as to jurisdiction there rendered merely retries the issue previously determined. There is no reason to expect that the second decision will be more satisfactory than the first."* (Italics ours.)

Incidentally, in said case of *Stoll v. Gottlieb, supra,* the Supreme Court refers to the case of *Fairbanks Steam Shovel Co. v. Wills,* 240 U. S. 642, 649, 60 L. Ed. 841, 36 S. Ct. 466, 36 Am. Bankr. Rep. 754, where the United States Supreme Court said: "The Bankruptcy Court is one of general jurisdiction."

We refer the Court to a recent case decided by the California District Court of Appeal, *Bank of America v. McLaughlin etc. Co.,* 40 Cal. App. (2d) 620, quoting from the syllabus as follows:

> "A bankruptcy court has the authority to pass upon its own jurisdiction, and also has the power to adjudicate title to property listed in the debtor's schedule."

Further quoting from the decision at pages 626-627, as follows:

> "The controversy between the parties on this point naturally divides itself into three headings: (1) the power of the bankruptcy court to pass upon its own jurisdiction; (2) its power to adjudicate title to property listed in the debtor's schedule; and (3) the effect of its decree determining more than one issue.
>
> (1) Preliminarily we start with the axiomatic observation that the decisions of the federal courts determining the jurisdiction of their own courts is controlling here as well as the decisions interpreting and declaring the purport and effect of their own judgments. Hence, when a judgment of a federal court is received in a state court it is to be accepted with the full faith and credit accorded that judgment in the jurisdiction where it was rendered and in the light of its interpretation in the federal decisions. This is the effect of the recent decision of the Supreme Court of the United States in *Stoll v. Gottlieb,* 305 U. C. 165 (59 Sup. Ct. 134, 83 L. Ed. 104), where it rejected the ruling of the Illinois state court refusing to accept certain decrees of a bankruptcy court as *res judicata* on the grounds that the bankruptcy court had no jurisdiction to enter the decrees.

* * * * * * * * *

"With this rule in mind we turn to the federal decisions as determinative of the first two questions presented. In *Chicot County Drainage Dist. v. Baxter State Bank,* 308 U. S. 371, 376 (60 Sup. Ct. 317, 319, 84 L. Ed. 329) (1940), the United States Supreme Court said:

* * * * * * * * *

'The court has the authority to pass upon its own jurisdiction and its decree sustaining jurisdiction against attack, while open to direct review, is res judicata, in a collateral action. (*Stoll v. Gottlieb,* 305 U. S. 165, 171, 172, 59 Sup. Ct. 134, 137, 83 L. Ed. 104.)'"

The learned District Judge in the case at bar relied at great length upon the case of *Ex parte Sawyer,* 124 U. S. 200, 31 L. Ed. 402, 8 S. Ct. 482, which was one of the cases relied upon unsuccessfully by respondent in *Stoll v. Gottlieb, supra,* and which is to be distinguished from the case at bar in this respect: In *Ex parte Sawyer, supra,* a restraining order was issued *ex parte* without notice, against officers of the municipality. The officers of the municipality never appeared in the proceeding out of which the restraining order was issued. In other words, the officers of the municipality had never had their day in court, and the issue of jurisdiction of the subject matter and of the person had never been raised by them. The Supreme Court points out that where a person is served with process, if he feels that such process is issued out of a court that does not have jurisdiction, he may disregard the same, and thereafter, when the same is sought to be enforced against him, he may then raise the question of

lack of jurisdiction. (*Baldwin v. Iowa State Traveling Men's Ass'n, supra.*) But if he appears in said action and raises the question of jurisdiction and the objection to the jurisdiction is overruled, it is incumbent upon him to carry said issue to the highest tribunal, because once said matter becomes final, either by a decision of the highest tribunal, or because of the failure to raise such question, that issue can no longer be raised.

In said case of *Ex parte Sawyer, supra,* there were two dissenting opinions, one by Mr. Chief Justice Waite and one by Mr. Justice Harlan. We quote from the language of the dissent of the Chief Justice, as follows, at page 223:

> "If the court can take jurisdiction of such a case under any circumstances, it certainly must be permitted to inquire, when a bill of that character is filed, whether the case is one that entitles the party to the relief he asks, and, if necessary to prevent wrong, in the meantime, to issue in its discretion a temporary restraining order for that purpose. Such an order will not be void, even though it may be found on examination to have been improvidently issued. While in force it must be obeyed, and the court will not be without jurisdiction to punish for its contempt. Such, in my opinion, was this case; and I therefore dissent from the judgment which has been ordered."

In this connection we quote from the case of *Stoll v. Gottlieb, supra,* as follows, at 305 U. S., page 177:

> "We do not review these cases as we base our conclusion here on the fact that in an actual controversy the question of the jurisdiction over the subject matter was raised and determined adversely to the respond-

ent. That determination is *res adjudicata* of that issue in this action, whether or not power to deal with the particular subject matter was strictly or quasi-jurisdictional."

In the case of *Jennings v. U. S.*, 264 Fed. 399, which was a case where the United States District Court issued an injunction, it is said:

"Another reason why the objections of Mr. Jennings to the jurisdiction of the court below to issue the order of injunction in the equity suit are not tenable is that he is estopped from successfully objecting to that jurisdiction by the adjudication which the court necessarily made that it had jurisdiction when it issued the order of injunction on notice to him of the hearing on motion for it, and by his failure to appeal from it within the time fixed for his appeal by the acts of Congress."

We also refer to the recent case of *Sunshine Anthracite Coal Co. v. Adkins,* 310 U. S. 381, 84 L. Ed. 1263, 60 S. Ct. 907, quoting therefrom at 84 L. Ed., p. 1276, as follows:

"* * * The suggestion that the doctrine of *res judicata* does not apply unless the court rendering the judgment had jurisdiction of the cause is sufficiently answered by *Stoll v. Gottlieb,* 305 U. S. 165, 83 L. Ed. 104, 59 S. Ct. 134, 38 Am. Bank. Rep. (N. S.) 76, and *Treinies v. Sunshine Min. Co.,* 308 U. S. 66, *ante,* 85, 60 S. Ct. 44. As held in these cases, in general the principles of *res judicata* apply to questions of jurisdiction as well as to other matters—*whether it be jurisdiction of the subject matter or of the parties.*"

Another recent decision of the United States Supreme Court further supports appellant's contention. In the case of *Robert H. Jackson, Atty. Gen. of U. S. etc. v. Irving Trust Co. et al.,* 85 L. Ed. (Adv. Op.) 310, it was held:

> (Syl.) "An unappealed decree of a Federal District Court * * * is not subject to collateral attack upon a subsequent motion * * * to have it set aside upon the ground that the court was without jurisdiction * * * where the court on the trial, although it did not consider the jurisdictional question as such, denied a motion made to dismiss the suit * * * and all the issues necessary to a determination of the right to maintain the suit were before the court in that suit.
>
> "Whether a particular issue was actually litigated is immaterial on the question of the conclusiveness of a decree, where there was full opportunity to litigate it, and it was adjudicated by the decree."

We also wish to refer the Court to the recent case of *Sampsell v. Imperial Paper & Color Corp.,* 85 L. Ed. (Adv. Op.) 797, at p. 799, to the effect that the order of a Referee cannot be collaterally attacked where no appeal has been taken therefrom.

Also to the recent case of *Pittsburgh Plate Glass Co. v. National Labor Relations Board,* 85 L. Ed. (Adv. Op.) 771, at p. 779 to the effect that the entry of an order upon stipulation and consent does not in any wise detract from its force and effect.

Also to the case of *Swift & Co. v. United States,* 276 U. S. 311, 72 L. Ed. 587, 48 S. Ct. 311, from which we quote at 276 U. S. 326, as follows:

> "It is contended that the Supreme Court lacked jurisdiction because there was no case or controversy within the meaning of §2 of article 3 of the Constitution. * * * The defendants concede that there was a case at the time when the Government filed its petition and the defendants their answers; but they insist that the controversy had ceased before the decree was entered. The argument is that, as the Government made no proof of facts to overcome the denials of the answers, and stipulated both that there need be no findings of fact and that the decree should not constitute or be considered an adjudication of guilt, it thereby abandoned all charges that the defendants had violated the law; and hence the decree was a nullity." * * * "Moreover, the objection is one which is not open on a motion to vacate. * * * On a motion to vacate, the determination by the Supreme Court of the District that a case or controversy existed is not open to attack."

Also, at page 324, as follows:

> "But 'a decree, which appears by the record to have been rendered by consent, is always affirmed, without considering the merits of the cause.' Nashville, C. & St. L. R. Co. v. United States, 113 U. S. 261, 266, 28 L. Ed. 971, 973, 5 Sup. Ct. Rep. 460. * * * Where as here, the attack is not by appeal or by bill of review, but by a motion to vacate, filed more than four years after the entry of the decree, the scope of the enquiry may be even narrower."

Quoting, further, at page 372:

> "If the court erred in finding in these allegations a basis for fear of future wrong sufficient to warrant an injunction, its error was of a character ordinarily remediable on appeal. Such an error is waived by the consent to the decree. United States v. Babbitt, 104 U. S. 767, 26 L. Ed. 921; McGowan v. Parish, 237 U. S. 285, 295, 59 L. Ed. 955, 963, 35 Sup. Ct. Rep. 543. Clearly it does not go to the power of the court to adjudicate between the parties."

It was likewise error for the District Court to go behind the order of injunction, inasmuch as the only issue before it was the question of contempt, and whether or not the appellees had committed a contempt by violating the order of injunction.

> *Remington on Bankruptcy* (5th Ed.), Vol. 7, Sec. 3043.

Also:

> *Remington on Bankruptcy* (5th Ed.), Vol. 5, Sec. 2428.

II.

The Appellee, Bolsa Chica Oil Corporation, Was Estopped From Questioning the Order of Injunction by Reason of Its Consent to the Making Thereof.

POINT 6. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt), for the reason that respondents are estopped from asserting such objections by virtue of their having submitted themselves to the jurisdiction of the bankruptcy court by stipulating that the injunction might be entered against them, by cross-examining the witnesses and otherwise participating in the proceedings against them.

POINT 7. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt) for the reason that respondents are estopped from asserting such objections by virtue of their having failed to taken an appeal or review from the injunctive proceedings before the Referee.

POINT 8. The District Court erred in failing to hold that any purported reservation of jurisdictional objections by the respondents was waived and nullified by the effect of the general appearance made by respondents in stipulating that the injunction might be entered against them and by approving the order of injunction not only as to form but as to contents as well.

The appellee, Bolsa Chica Oil Corporation, had the right to submit to the Bankruptcy Court's jurisdiction, which it did in this case. The evidence in this case shows that the appellee, Bolsa Chica Oil Corporation, consented to and stipulated to such order of injunction. Such consent and stipulation are evidenced by the following references to the record: [Tr. p. 57 and pp. 150-160] and quoted under Point I of this brief.

The complete testimony before the Referee leading up to the order of injunction of May 15, 1940, is not contained in the record for the reason that appellee, Bolsa Chica Oil Corporation, having stipulated thereto, and such stipulation and consent being evidenced by the Referee's certificate, and such order being based upon such consent, appellant did not consider that such evidence was necessary to be included in the transcript on appeal, although the reporter's transcript of such evidence and proceedings is in the possession of the clerk of the above court.

However, the principal question on this appeal is whether the Referee had jurisdiction to make the order of injunction and to issue the certificate of contempt.

The record clearly indicates that the Referee would not have signed the order and would not have made the terms of the injunction as broad as they are were it not for the statements of the appellee, Bolsa Chica Oil Corporation, that it would be bound by the order and that it would not take a review of such order. The Referee stated that if it were not for such statement of agreement not to review, he would want to give the matter further consideration before making such order. [Tr. p. 156.]

It is a well established point of law that a person who consents to the making of an order cannot question the power and jurisdiction of the court thereafter. By his consent and stipulation he recognizes the authority of the Court to make the same.

Semple v. Wright, 32 Cal. 659;

Morrow v. Learned, 76 Cal. App. 538;

Jackson v. Brown, 82 Cal. 275;

Fitzgerald v. Terminal Dev. Co., 11 Cal. App. (2d) 126.

It is appellant's contention that the appellee, Bolsa Chica Oil Corporation, by joining in the preparation of said order of injunction [Tr. p. 154], and by stipulating to the same in open court, virtually asked that the bankruptcy court give it relief and exercise its power. In this connection we refer the Court to 3 *Cal. Jur.,* p. 12, as follows:

> "In determining whether an appearance is general or special, *the characterization given it by the party is of no consequence whatever.* * * * On the other hand, if he appears and asks for any relief which could only be given a party in a pending case, *or which itself would be a regular proceeding in the case, it is a general appearance no matter how carefully or expressly it may be stated that the appearance is special.*" (Italics ours.)

Upon the hearing before the Referee the questions to be decided were whether the manner in which the appellee, Bolsa Chica Oil Corporation, was drilling its "Petroleum Well" would result in a trespass and damage to appellant's property, and whether to issue an order of in-

junction, enjoining such redrilling of said "Petroleum Well" in such a manner as would result in a trespass and injury to the property of the appellant. In connection with such issues, it was necessary to decide how close appellee, Bolsa Chica Oil Corporation, should drill its well to the well of appellant, the kind of circulating fluid to be used, *et cetera*. By its stipulation, appellee, Bolsa Chica Oil Corporation, asked the Court to make such determination in accordance with the stipulation.

In the proceeding before the Referee, the appellee, Bolsa Chica Oil Corporation, offered to enter into a stipulation that an injunction be issued in accordance with the agreement of appellant and appellee, Bolsa Chica Oil Corporation. In the written stipulation that followed, a recital appears to the effect that by virtue of entering into said stipulation the appellee, Bolsa Chica Oil Corporation, did not concede the general jurisdiction of the Bankruptcy Court. This expression would appear inconsistent with the submission to jurisdiction by said appellee. Quite obviously the purpose and effect of such recital was to limit the appearance of the appellee, Bolsa Chica Oil Corporation, to the particular matter of the injunction and not to submit to the general jurisdiction of the Court for other purposes as well. Furthermore, it is well settled that a general appearance by a party-litigant waives any objection that such party-litigant may have to the jurisdiction of the Court over such party-litigant. Having submitted itself to the jurisdiction of the Bankruptcy Court by participating in the proceedings, by the cross-examination of witnesses by offering to stipulate to the issuance of the order of injunction, by agreeing not to review the stipulated order of injunction, and by actually

stipulating to the issuance of such injunction, the appellee, Bolsa Chica Oil Corporation, thus forever concluded the question of the Court's jurisdiction over it, irrespective of any subsequent attempt to denominate such procedure as being purely a special appearance for the purpose of questioning the Court's jurisdiction. In other words, a party-litigant may question the jurisdiction of the Court, but while doing so, it may not ask the Court for affirmative relief and yet claim not to have submitted itself to the Court's jurisdiction.

In the case of *Burrows v. Burrows,* 10 Cal. App. (2d), 749, 750, the Court said:

> "It is the well-settled rule that if a party defendant raises any question other than that of jurisdiction or asks for any relief which can only be granted upon the hypothesis that the court has jurisdiction of his person, his appearance is general, though termed special, and he thereby submits to the jurisdiction of the court as completely as if he had been regularly served with summons. (Security Loan & Trust Co. v. Boston & South Riverside Fruit Co., 126 Cal. 418 (58 Pac. 941, 59 Pac. 296); Olcese v. Justice's Court, 156 Cal. 82 (103 Pac. 317).)"

We also refer the Court to the case of *Feldman Investment Co. v. Connecticut Life Insurance Co.*, 78 Fed. (2d) 838, from which we quote as follows:

> "An offer to confess judgment constitutes a general appearance and waives objections to jurisdiction of the person."

In 6 *Corpus Juris Secundum,* section 1(c), page 9, it is said:

> "* * * A defendant appearing specially to object to the jurisdiction of the court must, as a general rule, keep out of court for all other purposes and limit his appearance to that particular question. Consequently, if, after he has appeared specially to question the jurisdiction, defendant fails to limit his appearance to a consideration of that particular question, or takes any step consistent with the hypothesis that the court has jurisdiction of the cause and the person, the special appearance is thereby converted into a general appearance irrespective of whether or not it is by its terms limited to a special purpose, *and an attempted reservation of the special appearance and rights thereunder is wholly ineffectual.*" * * * (Italics ours.)

Citing:

Benedict v. Seiberling, 17 Fed. (2d) 841 (D. Ct. Ohio);

O'Brien v. Lashar, 273 Fed. 521 (C.C.A., Conn.);

Payne v. Pullan, 44 Cal. App. 728.

We also wish to refer the Court to Vol. 3, *Am. Jur.,* section 12, p. 790, as follows:

> "If an appearance is in effect a general one, the fact that the party making it characterizes it as a special appearance or that it is expressly limited by its terms as special, does not prevent it from being general, as all appearances are presumed to be general."

Further, quoting 3 *Am. Jur.*, section 42, p. 811:

> "And in an action is a federal court, where the defendant appears specially for the purpose of raising the question of jurisdiction over his person, is fully heard upon such question, and, upon the overruling of his motion to quash service, takes no further part in the case and seeks no review, a judgment subsequently entered against him on the merits is *res judicata* on the question of jurisdiction and is not subject to be collaterally attacked on that same ground when issued on in another state." (Citing *Baldwin v. Iowa State Traveling Men's Ass'n, supra.*)

We further refer the Court to the case of *State ex rel. Bingham v. District Court,* 80 Mont. 97, 257 Pac. 1014 where the court stated:

> "In short, the rule is that counsel cannot asservate and reprobate in the same breath; he cannot acknowledge that the cause is in court for certain purposes and at the same time assert that the court is without jurisdiction to proceed in the cause in any manner. In the situation in which counsel found himself in March, he was at a juncture of the main highway and a byway; he could not travel both, but was compelled to choose which way he would go; having chosen the highway leading to a final determination of the action, he was barred from entering also upon the byway or thereafter returning to it."

The evidence in this case shows that appellee, Bolsa Chica Oil Corporation, not only participated in the hearing

by cross-examining the witnesses of the trustee [Tr. pp. 57 and 150], but helped to prepare the order of injunction and stipulated to such order. Said order was approved not only as to form but also as to contents. [Tr. p. 32]. Appellant's contention is that appellee, Bolsa Chica Oil Corporation, could not in one breath say "You can make this order," and at the same time say "You have no right to make it."

Furthermore, it is appellant's contention that the question of whether or not consent was given is a question of fact (*Remington on Bankruptcy* (5th Ed.), Vol. 5, p. 336) and the Bankruptcy Court having found that consent was given and no appeal having been taken, said matter was forever concluded against the appellees.

It must be strongly emphasized that the consent of the appellee, Bolsa Chica Oil Corporation, was not necessary, since the Bankruptcy Court may, in any event, issue injunctions to prevent interference or damage to the property in its possession. But even assuming that the consent of appellee, Bolsa Chica Oil Corporation, was necessary, we feel that it consented by virtue of its participation in the injunction procedings and by virtue of its stipulation to said order of injunction. Whether the appellee, Bolsa Chica Oil Corporation consented or not, is a question of fact. The finding by the Referee that there had been such consent, where supported by evidence, should not be disturbed. *Remington on Bankruptcy* (5th Ed.), Volume 5, Section 2197, p. 336 and *In re Traylor,* 27 F. Supp. 778, 779 (D. C. Ky.)

III.

The Bankruptcy Court, Both Under the Bankruptcy Act Itself, and as a Court of Equity, Has the Inherent Power to Protect Property in Its Custody and to Enjoin Any Injury or Threatened Injury Thereto.

POINT 4. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt) for the reason that the bankruptcy court is a court of equity and as such has inherent power to enjoin threatened harm to, or interference with, the property in custody of the bankruptcy court.

POINT 5. The District Court erred in sustaining objections to the jurisdiction of the Referee to issue the injunction (the violation of which was the basis for the Certificate of Contempt), for the reason that the bankruptcy court is given power, under Section 2(15) of the Bankruptcy Act of 1938 to enjoin any threatened harm to, or interference with, the property in custody of the bankruptcy court.

The bankruptcy court under section 2(15) of the Bankruptcy Act has the power to make such orders and issue such process as may be necessary properly to administer any property within its custody, control or jurisdiction. The Bankruptcy Court is also a court of equity and has the inherent power by injunction to protect any property within its custody or control.

See *Collier on Bankruptcy* (14th Ed.), §2.61, Vol. 1, p. 253, as follows:

> "Clause (15)" (of section 2(a) of Bankruptcy Act) "is an omnibus provision, phrased in such general terms as to be the basis for a broad exercise of power

in the due administration of a bankruptcy proceeding. The most important and frequent example of this exercise is the use of the power *to enjoin or restrain the actions of others.* While such power is probably inherent in the bankruptcy court as a court of equity, clause (15) gives it express legislative sanction."

"The essential purpose of §2a(15) is to give the court power to protect its custody of the estate and the administration thereof."

See, also, Collier on Bankruptcy (14th Ed.), Vol. 1, §2.65 from which we quote at page 280, as follows:

"The injunctive power, when exercised, is subject to the same rules and limitations as in the case of other equitable writs of injunction, and *its use is available to prevent the infliction of threatened or imminent,* but not mere possible, *injury.*" (Italics ours.)

In the *Matter of Baldwin,* 291 U. S. 610, the Supreme Court said:

"To protect its jurisdiction from interference that court (the bankruptcy court) may issue an injunction. The power is not peculiar to bankruptcy or to the federal courts. It is an application of the general principle that where a court of competent jurisdiction has, through its officers, taken property into its possession the property is thereby withdrawn from the jurisdiction of other courts. Having possession, the court may not only issue all writs necessary to protect its possession *from physical interference,* but is entitled to determine all questions respecting the same." (Italics ours.)

In *Steelman v. All Continent Corp.,* 301 U. S. 172, 57 S. Ct. 705, 81 L. Ed. 1085, the United States Supreme Court, referring to section 2a(15) of the Bankruptcy Act, said:

> "Referring to these statutes, this court has said that 'the power to issue an injunction when necessary to prevent the defeat or impairment of its jurisdiction is * * * inherent in a court of bankruptcy, as it is in a duly established court of equity.'"

A bankruptcy court under Sec. 2a(15) and in the exercise of its equitable power, may issue injunctions and restraining orders to preserve the assets of the bankrupt's estate.

> *In re Consumers' Albany Brewing Co.* (D. C., N. Y.), 224 F. 235.

Labor unions may be enjoined from interfering with the operation of a brewery by a debtor in corporate reorganization, notwithstanding the Norris-La Guardia Anti-Injunction Act.

> *In re Cleveland and Sandusky Brewing Co.* (D. C. Ohio), 11 F. Supp. 198, 29 Am. B. R. (N. S.) 393, 127 A. L. R. 873.

In this connection, we again wish to refer the Court to the case of *Swift & Co. v. United States, supra,* quoting therefrom at 276 U. S., p. 326, as follows:

> "The argument ignores the fact that a suit for an injunction deals primarily, not with past violations, but *with threatened future ones;* and *that an injunction may issue to prevent future wrong, although no right has yet been violated.* Vicksburg Waterworks

Co. v. Vicksburg, 185 U. S. 65, 82, 46 L. Ed. 808, 815, 22 Sup. Ct. Rep. 585; Pierce v. Society of Sisters, 268 U. S. 510, 536, 69 L. Ed. 1070, 1078, 39 A. L. R. 468, 45 Sup. Ct. Rep. 571."

Also, at page 331, as follows:

"If the court, in addition to enjoining acts that were admittedly interstate, enjoined some that were wholly intrastate and in no way related to the conspiracy to obstruct interstate commerce, it erred; and had the defendants not waived such error by their consent, they might have had it corrected on appeal. But the error, if any, does not go to the jurisdiction of the court. *The power to enjoin includes the power to enjoin too much.*" (Italics ours.)

We refer the Court to the case of *Morehouse v. Giant Powder Company,* 206 Fed. 24, where it is said:

"A court of bankruptcy has jurisdiction to grant an injunction restraining any act which will interfere with the administration of the bankruptcy law against any person within its jurisdiction, whether a party to the bankruptcy proceedings or not."

In said cited case, Morehouse, the party found in contempt, was not a party to the bankruptcy procedings; was not named in the injunction in the bankruptcy court; yet the court, at pages 28 and 29 of this case, states as follows:

"It is contended that the plaintiffs in error were not and could not have been made parties to the bankruptcy proceedings, and that, therefore, the District Court had no jurisdiction over them, and no power to enjoin them. But section 2, cl. 15, gives the bank-

> ruptcy court power to issue injunctions against persons within the court's jurisdiction, whether parties to the bankruptcy proceedings or not, to prevent the transfer or disposition of any part of the bankrupt's property. * * * 'To render a person amenable to an injunction, it is neither necessary that he should have been a party to the suit in which the injunction was issued, nor to have been actually served with a copy of it, so long as he appears to have had actual notice.' "

The evidence in this case clearly shows, that on two occasions previous to the hearing on the contempt citation, the property of the bankrupt estate had been seriously interfered with and damaged, once due to the redrilling operations of the Termo Company, (a neighboring operator of both appellant and appellee, Bolsa Chica Oil Corporation), which conpletely destroyed the well of the bankrupt estate, necessitating its redrilling at a cost of $80,000.00 [Tr. p. 56]; and second due to the redrilling operations of the appellee, Bolsa Chica Oil Corporation, which necessitated remedial operations, to again place said well on production, damaging appellant to the extent of $12,540.00. [Tr. p. 62]. The evidence in this case shows that both the well of the appellant and the well of the appellee, Bolsa Chica Oil Corporation, as well as the well of the Termo Company, are bottomed under the ocean off the shore at Huntington Beach; that said wells are operated under easements from the State of California; that appellee, Bolsa Chica Oil Corporation, was bound by the same restrictions and conditions, in the operation of its well, as appellant [Tr. pp. 124-125]; that appellee, Bolsa Chica Oil Corporation, without secur-

ing the consent of the State of California [Tr. p. 154], commenced operations to redrill its "Petroleum Well"; that said appellee intended to re-drill said well under State easement 290-1 so that at the point where it struck the oil sands its well would be within a distance of less than one hundred feet from the "Huntington Shore" well of appellant being operated under State easement 309-2A [Tr. p. 125]; that the regulations of the State of California required it to be at least a distance of 200 feet from any other well [Tr. p. 95]; that appellee intended to (and actually did thereafter) use mud as a drilling fluid instead of crude oil as required by the regulations of the State of California [Tr. p. 95]; that the oil sands being of a porous and migratory nature would cause the mud used in redrilling said well of the appellee, Bolsa Chica Oil Corporation, to enter the "Huntington Shore Well" of the appellant, and thereby damage said well of appellant [Tr. p. 57, pp. 180-184]; that this threatened destruction was not based upon a mere possibility, as evidenced by the fact that it had already happened in the case of the redrilling of the Termo Well which took place before operations were commenced on the re-drilling of the well of the appellee, Bolsa Chica Oil Corporation, and that it also occurred when the operations were conducted on the well of said appellee.

Under such a showing it was competent for the Bankruptcy Court to issue its injunction requiring drilling operations to be conducted on the well of the appellee, Bolsa Chica Oil Corporation, in the manner required by law, so that they would not damage the property of the bankrupt estate. The appellee, Bolsa Chica Oil Corporation recognized that the request of the bankrupt estate was a reasonable one, and with the assistance of the engi-

neers of the appellee, Bolsa Chica Oil Corporation, it collaborated in the drafting and preparation of the order of injunction, to which it stipulated, and which it approved. [Tr. pp. 150-160.] The Bankruptcy Court did not interfere with the operation of the property of the appellee, Bolsa Chica Oil Corporation, but only enjoined such operation to the extent that it would damage appellant's well or interfere with the operation thereof by the Trustee. The right of the appellee, Bolsa Chica Oil Corporation, to redrill its well, did not include the right to destroy appellant's property rights and prevent future operation of appellant's well. Hence, in issuing the order of injunction against the appellee, Bolsa Chica Oil Corporation, the Referee was within the proper exercise of the equitable jurisdiction of the Bankruptcy Court.

In order for the Court to have a better understanding of the situation confronting the appellant and the appellee, Bolsa Chica Oil Corporation, in its operations, appellant wishes to call the Court's attention to the fact that there are a large number of wells, the surface locations of which are situated on the land side of the beach at Huntington Beach; that some of said wells are located as much as five blocks from the ocean beach; that said wells were originally drilled without the consent of the State of California, and without the consent of the Standard Oil Company of California, which owns the wells located on the beach at Huntington Beach; and that all of said wells, in order to be bottomed under the ocean, had to traverse the land of the Standard Oil Company of California, and

had to traverse the land of various other property owners in the Huntington Beach area; that said wells cross each other or cross within a short distance of each other in reaching the oil sands; that after said wells had been drilled, injunction suits were filed by the Standard Oil Company of California and the State of California; that as a result of such suits, a settlement was effected wherein and whereby easements were granted by the State of California upon a royalty basis to produce oil from the ocean bottom; that all of said easements are in identical form to that of appellant [Tr. p. 97]; that under said settlement, it was further provided that all of said operators should become members of an association called the "Huntington Beach Townsite Association" [Tr. p. 125] and that said association, as a representative of such operators whose wells were bottomed under the ocean and whose wells crossed the lands of the Standard Oil Company of California, would and did put up a bond to indemnify the Standard Oil Company of California for any damage to its wells by reason of any of said operators' wells interfering with the production of the wells of the Standard Oil Company of California in traversing the latter's lands. In other words, under said arrangement, said ocean bottomed oilfield was constituted a common pool in which each of said well owners was given an easement along and through which it could construct a cylindrical hole, for the purpose of extracting and producing oil [Tr. pp. 135-150]; that for the purpose of avoiding damage to each other's wells, regulations were adopted by the State re-

quiring the cylindrical hole of each operator to be a certain distance apart from the others, and that oil be used as a drilling fluid instead of mud so as to prevent mud from interfering with the operations of any of said other wells [Tr. p. 95]; that the appellee, Bolsa Chica Oil Corporation, was acquainted with all of the foregoing conditions, and because it knew that the consent of the State of California would not be given to the re-drilling of its wells in such manner, arbitrarily proceeded with such re-drilling without such consent. [Tr. p. 154.]

The learned District Judge indicated that an injunction will not issue for a threatened trespass but only for an actual trespass. We quote his language at page 8 of said reporter's transcript of the argument before him, lines 21 to 24, as follows:

> "But there is no case of that character in the federal courts holding that we can enjoin in advance of the doing of a tortious act."

The law is clearly settled that a litigant does not have to wait for a trespass that will cause irreparable injury to take place before taking any action, but where any threat of an act which will cause such damage is made, grounds for injunction exist. In this connection, we refer the Court to 24 *Cal. Jur.* 699 from which we quote as follows:

> "Originally, the right to restrain by injunction mere acts of trespass seems to have been confined to instances where the injury was to the freehold, in the

nature of waste, such as the taking of wood or timber, extracting valuable minerals and the like. But the jurisdiction of equity is not now to be considered as confined alone to such cases; * * *. Thus a person may be protected in the enjoyment of an easement or right of way where his rights are *threatened.*" (Italics ours.)

In *Slater v. Pacific American Oil Co.,* 212 Cal. 649, the plaintiff obtained an injunction and damages against defendant for allowing certain injurious substances to be carried from defendant's wells onto plaintiff's property.

At page 655 of the foregoing case, the Court said:

"However indefinite the evidence may be as a standard for the measurement of damages, our examination of the record satisfies us that *plaintiff sufficiently established that some portion of the oil, salt and other hydrocarbon substances causing the injury to his land had come from the operation of the defendant's wells.* This showing is sufficient to warrant the granting of *injunctive relief.*" (Italics ours.)

Further, the Court says at page 655:

"It is settled that a trespass of a continuing nature, the constant recurrence of which renders the remedy at law inadequate, unless by a multiplicity of suits, affords sufficient ground for relief by way of injunction. (United Railroads v. Superior Court, 172 Cal. 80, 84 (155 Pac. 463, 464); Parker v. Larsen, 86 Cal. 236 (21 Am. St. Rep. 30, 24 Pac. 989).)"

We also refer the Court to the case of *Tristam v. Marques,* 117 Cal. App. 393, from which we quote at page 397 as follows:

> "The right to restrain by injunction may properly be exercised whenever from the particular nature of the property affected by the trespass the injury sustained cannot be remedied by an action at law. (*Roberts v. Hall,* 147 Cal. 434 (82 Pac. 66); High on Injunction, 4th Ed., 661; *Zierath v. McCann,* 20 Cal. App. 561 (129 Pac. 808).)"

In the case of *Parker v. Larsen,* 86 Cal. 236, the plaintiff was held to be entitled to injunctive relief where defendant allowed water to percolate or flow upon plaintiff's land.

In *Union Oil Co. v. Reconstruction Oil Co.,* 20 Cal. App. (2d) 170, 182, the plaintiff sought to enjoin defendants from slant-drilling an oil well under his land. The action was brought before the plaintiff had any cause of action for damages. The Court held the acts of defendant constituted a trespass which could be enjoined.

In *Union Oil Co. v. Domengeaux,* 30 Cal. App. (2d) 266, it was held that slant-drilling of an oil well under plaintiff's land was a trespass that could be enjoined. The Court held further that in cases of subsurface trespass the injury is irreparable in itself, citing with approval, *Richards v. Dower,* 64 Cal. 62 (28 Pac. 113).

IV.

The Bankruptcy Court Had the Right to Adjudge the Appellees in Contempt for Interfering With the Property of the Bankrupt Estate, Even Though No Injunction Had Ever Been Issued by the Bankruptcy Court.

POINT 9. The District Court erred in not considering the Certificate of the Referee and not hearing any evidence offered in addition thereto, because said evidence would have shown that respondents interfered with the property in the custody of the bankruptcy court and did so wilfully and intentionally, and with full knowledge of the harm being done the property in custody of the bankruptcy court; and that such conduct constitutes contempt of court even had there been no injunction.

The filing of the bankruptcy proceeding constitutes a *caveat* to the entire world. *Acme Harvester Co. v. Beekman Co.*, 222 U. S. 300, 56 L. Ed. 208, 32 S. Ct. 96; *Taylor v. Sternberg*, 293 U. S. 470, 79 L. Ed. 599, 55 S. Ct. 260; *Gross v. Irving Trust Co.*, 289 U. S. 342, 77 L. Ed. 1243, 53 S. Ct. 605; *Taubel-Scott-Kitzmiller Co. v. Fox*, 264 U. S. 426, 68 L. Ed. 770, 44 S. Ct. 396. By such *caveat* all persons are warned, admonished and enjoined from interfering with the property of the bankrupt estate. From the time of the filing of the petition in bankruptcy the property is in *custodia legis*. *Lazarus v. Prentice*, 234 U. S. 263, 58 L. Ed. 1305, 34 S. Ct. 851; *Mueller v. Nugent*, 184 U. S. 1, 46 L. Ed. 405, 22 S. Ct. 269; *Straton v. New*, 283 U. S. 318, 75 L. Ed. 1060, 51 S. Ct. 465. The property being in *custodia legis*, the

bankruptcy court has the inherent power to protect such property under its custody and jurisdiction, and any person knowing that such property is in the custody of the court, who willfully interferes therewith, is guilty of contempt.

In this connection, we quote from *Remington on Bankruptcy* (5th Ed.), Vol. 7, Sec. 3028, pp. 123, 124, as follows:

> "Interference with property in the custody of the bankruptcy court is of course a contempt. * * * And such interference is punishable as contempt even though no injunction be issued."
>
> *Clay v. Waters,* 178 F. 385 (C. C. A., Mo.);
>
> *In re Wilk,* 155 F. 943 (D. C., N. Y.).

We also wish to refer the Court to 23 *R. C. L.,* Sec. 70, p. 64, as follows:

> "It is the duty of a court appointing a receiver to protect him in the discharge of his duties and in the control and possession of the property in his custody as such against anyone interfering therewith, whether a party to the receivership proceeding or not, and whether he claims paramount to or under the right which the receiver was appointed to protect. The possession by the receiver is that of the court, and consequently if any person without leave intentionally interferes with such possession, he necessarily commits a contempt of court, and is liable to punishment therefor." *In re Tyler,* 149 U. S. 164, 37 L. Ed. 689.

At the time of the hearing on the petition why the appellees should not be certified for contempt, it was shown that the appellees had consented to an order requiring appellee, Bolsa Chica Oil Corporation, to re-drill its well in a certain manner; that such order was prepared with the assistance of the engineers of said Bolsa Chica Oil Corporation. Assuming, for the purpose of argument, that such order might have been beyond the authority of the Bankruptcy Court, it at least constituted a contract, and a rule of conduct between appellant and appellee, Bolsa Chica Oil Corporation. By such contract it was established what an ordinary prudent person should and should not do; it was established that if such course of conduct was not followed the bankrupt's property would be destroyed and the administration of the bankrupt estate necessarily interfered with. At such hearing on contempt proceedings before the Referee, it was shown that the appellee, Bolsa Chica Oil Corporation, its president, Thomas W. Simmons, its superintendent, Allan A. Anderson, and its attorney, William H. Cree, knew that the Termo Company had, by doing the very things which it was shown on the contempt hearing that said appellee, Bolsa Chica Oil Corporation, was doing, irreparably damaged the well of the bankrupt estate; that subsequent to the making of such stipulated order of injunction, and in violation thereof, the appellee, Bolsa Chica Oil Corporation, had caused a column of mud 3700 feet high to enter the well of the appellant and that notwithstanding such stipulated order and notwithstanding the notice and knowl-

edge that it had of the damage which would necessarily ensue to the property of the bankrupt estate, it proceeded, aided and abetted by the other appellees, to carry on operations in the same manner as prohibited by the order of injunction, and in the same manner that had caused damage to the bankrupt's well on two previous occasions. The evidence clearly shows that all of said appellees knew that said property was in the custody of the bankruptcy court; that all the appellees knew and were presumed to know that the requirements of the State of California were to use oil and not mud as a circulating fluid in the re-drilling of any well in said field. [Tr. p. 95]. We feel that a clearer case of interference with the property of the bankrupt estate would be difficult to prove.

We respectfully urge that under the law as hereinbefore set forth, the order of the District Court should be reversed.

Respectfully submitted,

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JOSEPH J. RIFKIND,
By RAPHAEL DECHTER,
Attorneys for Appellant.

No. 9790.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE T. GOGGIN, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt,

Appellant,

vs.

BOLSA CHICA OIL CORPORATION, a corporation, THOS. W. SIMMONS, ALLAN A. ANDERSON, WILLIAM H. CREE, H. H. MCVICAR, C. M. ROOD, and M. M. MCCALLEN CORPORATION, a corporation,

Appellees.

Appellant's Reply to Brief of Appellees Bolsa Chica Oil Corporation, Thos. W. Simmons and Allan A. Anderson and the Supplementary Brief of Appellees William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation.

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PRELIMINARY STATEMENT.

In view of the fact that the appellees William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation, in their supplementary brief have adopted by reference the contents of the brief of appellees Bolsa Chica

Oil Corporation, Thos. W. Simmons and Allan A. Anderson, we shall devote the larger portion of this brief to replying to the brief of the latter appellees, and shall devote attention to the additional arguments of the supplementary brief after first disposing of the brief of the appellees Bolsa Chica Oil Corporation, *et al.*

STATEMENT OF THE HISTORY OF THE CASE.

We note first that appellees have taken issue with certain matters contained in the statement of the history of the case contained in our opening brief. It will be noted that the statement contained in appellant's history of the case is borrowed from the certificate of contempt of the Referee. [Tr. 53 to 72.] This certificate of contempt of the Referee contains the only findings of fact ever made by the only tribunal that ever heard evidence. The hearing before the Honorable Leon R. Yankwich, District Judge, was one in which the District Court heard no evidence whatsoever and refused to receive any evidence. [Tr. 83 to 85.] Until the District Court hears the evidence, or until some direct review is taken from the findings of the Referee, the findings of fact of the Referee must be deemed to be presumptively correct. *General Order No. 47.*

Remington, Vol. 7, Sec. 3034, page 131;
Remington, Vol. 7, Sec. 3035, page 132.

ARGUMENT.

The Bankruptcy Court Was Fully Empowered to Issue the Injunctive Order Which Is the Basis of the Contempt Proceeding Herein Involved.

Appellees' first argument is directed to the contention that the bankruptcy court had no jurisdiction to make the order of injunction which was violated by appellees and gave rise to the contempt proceeding. Appellees contend that the injunction was beyond the power of the bankruptcy court. Yet appellees in searching for the jurisdictional powers of the bankruptcy court appear to have hunted every place but the one wherein the powers of the bankruptcy court are specifically enumerated, to-wit, the Bankruptcy Act. Appellees' brief fails even to mention Section 2a (15) of the Bankruptcy Act of 1938, which we cited again and again in our opening brief. This is a significant silence in the light of the fact that Section 2a (15) unequivocally vests the bankruptcy court with all of the jurisdiction necessary to sustain the injunctive order in this case.

The Bankruptcy Act provides, as follows:

> "§2a. Courts; Jurisdiction and Powers.—The courts of bankruptcy as defined in the previous chapter, namely, the district courts of the United States in the several states, the Supreme Court of the District of Columbia, the district courts of the several territories and possessions to which this title is, or may after July 1, 1898 be, applicable, and the United States court in the district of Alaska, are hereby made

courts of bankruptcy, and are hereby invested, within their respective territorial limits as established on July 1, 1898, or as they may be thereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings, in vacation in chambers and during their respective terms, as they were on July 1, 1898 or may be thereafter held, * * * (15) make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this title; * * *."

It is well established that this section vests the bankruptcy court with the power to enjoin or restrain the actions of any stranger who threatens to injure the property of the bankrupt estate. *Collier on Bankruptcy,* 14th Edition, Vol. 1 Sections 261 and 265.

In the Matter of Baldwin, 291 U. S. 610;

Steelman v. All Continent Corp., 301 U. S. 172, 57 S. Ct. 705, 81 L. Ed. 1085;

Morehouse v. Giant Powder Company, 206 Fed. 24.

These and other cases cited in our opening brief remain unanswered by appellees.

Appellees contend that the bankruptcy court acted in excess of its jurisdiction. To enjoin too much would not deprive the court of its jurisdiction—and failure to appeal on the extent of the injunction renders the injunction final and binding. Thus the United States Supreme Court in *Swift & Co. v. United States,* 276 U. S. 311 (326), 72 L. Ed. 587, 48 S. Ct. 311, held that:

"The power to enjoin includes the power to enjoin too much."

Appellees' arguments on lack of jurisdiction lack conviction unless appellees can show that Section 2a (15) of the Bankruptcy Act of 1938, is either void, unconstitutional or non-existent. Congress vested the bankruptcy court with the jurisdiction to restrain any interference with its administration of estates for the very good and obvious reason that without such authority the ends and purposes of bankruptcy administration could be defeated by outside interference. All of the cases passing upon the right of the court to enjoin interference even from strangers recite that even without the effect of Section 2a (15), the bankruptcy court would nevertheless be vested with the necessary jurisdiction to prevent interference, such jurisdiction always being inherent in a court of equity. A court of bankruptcy is a court of equity. *Continental Ill. Nat. Bank, etc. v. Chicago, Rock Island, etc. Ry. Co.*, 294 U. S. 648, 79 L. Ed. 1110, 55 Sup. Ct. 595.

Appellees contend that the injunction in this case was issued on "mere apprehension of injury". Appellees contend that at the time the injunction was issued "no injury was threatened, no invasion of appellant's property was imminent." We take issue with these broad statements which are unsupported by the record. The record reveals that appellee Bolsa Chica Oil Corporation was familiar with the damage done to appellant's well by the "Termo Well", which was occasioned by the use of mud. [Tr. 55, 56.] Testimony before the Referee showed that if mud was used, mud would be carried through the oil sands into appellant's well and would irreparably injure and damage said well. [Tr. 57.] As a result of the violation of the injunction by appellees, the use of mud in violation of such injunction, caused a column of mud to be raised in

the bottom of appellant's well and stopped production of said well. [Tr. 60.] The evidence further reflected that the violation of the injunction through the use of mud reduced the production of appellant's well from 260 barrels of oil per day to 160 barrels of oil per day. [Tr. 61.] And yet appellees unblushingly state "no injury was threatened, no invasion of appellant's property was imminent."

Again and again appellees reiterate that they were making but a lawful use of their own property and that the bankruptcy court had no authority to interfere. Page 120 of appellees' brief cites a number of inapplicable cases to support appellees' contention that they had the right to use their own property lawfully without interference from the bankruptcy court. Counsel for appellees have lost sight of the well-established doctrine, *sic utere tuo ut alienum non laedas,* which provides that it is unlawful for one to so use his property as to cause injury to another. This doctrine of liability even without negligence or fault was first announced in the famous case of *Ryland v. Fletcher,* L. R. 3, H. L. 330, and has been and is being followed by the California courts.

In *Green v. General Petroleum Corp.* (1928), 205 Cal. 328, 270 Pac. 952, 60 A. L. R. 475, defendant was held absolutely liable for damage done by an oil well "blow-out" covering plaintiff's property with oil, sand, mud, rocks, etc., despite the fact that defendant had exercise the utmost care. It was said:

> "Appellant contends that it was absolved from all liability for the damages to respondents' property under the finding of the trial court that it had exer-

cised due care and caution in its drilling operations. Respondents rely upon the application of the doctrine, *sic utere tuo ut alienum non laedas,* to the facts in the case. * * *

"The discovery and production of oil is a legitimate and lawful business, and when properly carried on and maintained, is not a nuisance *per se.* Under normal conditions, the drilling operations cause no invasion of the adjacent lands. The fact, therefore, that the well of appellant was properly put down and carefully cared for, appellant contends, eliminates the only factor in the case which would justify a judgment for respondents in the absence of negligence. We do not think so. The present care does not arise from either the conduct of a nuisance *per se,* or from an inevitable calamity or act of God, but presents a situation to which the doctrine of *sic utere tuo ut alienum non laedas* may be applied in its broad and fundamental import. The ancient maxim of jurisprudence is incorporated, in substance, in the statutory law of this state. The Civil Code provides (Sec. 3514): 'One must so use his own rights as not to infringe upon the rights of another.' Where one, in the conduct and maintenance of an enterprise lawful and proper in itself, deliberately does an act under known conditions, and, with knowledge that injury may result to another, proceeds, and injury is done to the other as the direct and proximate consequence of the act, however carefully done, the one who does the act and causes the injury should, in all fairness, be required to compensate the other for the damage done. The instant case offers a most excellent example of *an actual invasion* of the property of one person through the act of another."

See also the following cases which support and supplement *Green v. General Petroleum, supra:*

Nolla v. Orlando (1932), 119 Cal. App. 518, 6 Pac. (2d) 984;

Kall v. Carruthers, 59 Cal. App. 555, 211 Pac. 43 (1922);

McGrath v. Basich Bros. Const. Co., 7 Cal. App. (2d) 573, 46 Pac. (2d) 981 (1935).

Neither *Beauchamp v. United States,* 76 Fed. (2d) 663; or *American Bank & Trust Co. v. Federal Reserve Bank of Atlanta,* 67 L. Ed. 1153, 262 U. S. 643, cited by appellees are pertinent to the issues. Neither of these cases involve any interference with the property in the custody of the bankruptcy court other than that of normal competition. Neither involved threats of trespass. In the instant case appellee Bolsa Chica Oil Corporation had threatened to use a means of procedure in the drilling of its well which threatened physical injury to appellant's well. It is as much a trespass for appellee to make an underground invasion of appellant's property as it would be a trespass if such invasion were on the surface.

E. A. Bell v. Bell View Oil Syndicate, 24 Cal. App. (2d) 587, 76 Pac. (2d) 167;

Union Oil Company v. Mutual Oil Company, 19 Cal. App. (2d) 409, 65 Pac. (2d) 896.

The California court has held that it will enjoin subterranean trespass.

Union Oil Co. v. Reconstruction Oil Co., 20 Cal. App. (2d) 170, 66 Pac. (2d) 1215;

Union Oil Co. v. Domengeaux, 30 Cal. App. (2d) 266, 86 Pac. (2d) 127.

We find it difficult to comprehend appellees' impassioned plea for sympathy on page 10 of its brief, in which appellees submit "that a monstrous wrong was done to appellee; private rights were ruthlessly invaded and the referee in bankruptcy exceeded his power in granting such an injunction." It ill becomes appellees to complain of a "monstrous wrong" and a "ruthless invasion" in view of the fact that this so-called "monstrous wrong" and "ruthless invasion" came by express invitation from appellees themselves. It will be noted from the record that in the proceeding before the Referee, Mr. Warren S. Pallette, then and now counsel for appellees suddenly was inspired to end the proceedings by suggesting the injunction by stipulation. [Tr. 152 ff.] Accordingly, appellees present copious tears appear synthetically produced since nothing was contained in the order of injunction which was not suggested by appellees themselves and agreed to by appellees themselves. The only "monstrous wrong" that we are able to perceive is the contemptuous violation of the court's injunction and the contemptuous withdrawals by appellees of the word and integrity in which they agreed to the injunctive order. The only "ruthless invasion of private rights" that we perceive is the damage done by appellees to appellant's well despite the court's injunction and despite the knowledge that such action would result in irreparable damage and injury to appellant.

Appellees complain further that the referee lacked jurisdiction to issue the order of injunction because such order

of injunction was secured in a summary proceeding. The cases cited by appellees are all turnover cases against adverse claimants who did not consent to the proceedings against them. The facts of the instant case are distinguishable from the cited cases in that the referee in the instant case acted by injunction to prevent threatened trespass and injury to property within the custody of the court. As we have heretofore pointed out (and which has been entirely ignored by appellees) Section 2a(15) of the Bankruptcy Act of 1938, as well as the general powers adherent in a court of equity, furnish the authority upon which the bankruptcy court can and must act to protect the property in *custodia legis*. The instant case is not an adverse claimant case. It is truly a trespass case and is dissimilar from the adverse claimant cases in that in the latter the property involved is not in the possession of the court and the adverse claimant refuses to submit himself to the jurisdiction of the court. In the instant case the Referee in Bankruptcy acted to prevent appellees from going upon the property which was in the custody of the bankruptcy court and injuring the same. It is fundamental that the trespass by a subterranean invasion is as much a trespass as any other, and the cases are legion that have granted injunctive process to prevent subsurface trespass.

The District Court Erred in Permitting a Collateral Attack Made Upon the Injunctive Order, the Violation of Which Was the Basis for the Contempt Proceeding.

Appellees insist that the attack upon the jurisdiction of the Referee made before the District Court is a direct rather than a collateral attack. They argue further that the case of *Stoll v. Gottlieb,* 305 U. S. 165, 83 L. Ed. 104, 59 S. Ct. 134, is applicable only to cases involving collateral rather than direct attacks upon jurisdiction of the court. Appellees reach this conclusion by citing from the opinion in *Stoll v. Gottlieb,* wherein the Supreme Court distinguishes the *Stoll* case from that of *Vallely v. Northern F. & M. Ins. Co.,* 254 U. S. 348, 65 L. Ed. 297, 41 S. Ct. 116. The Supreme Court held that the *Vallely* case "is inapplicable here because there was not an actually contested issue and order as to jurisdiction. The case is also distinguishable because the motion to vacate was made in the same bankruptcy proceeding as the order". Appellees thereupon argue that this latter distinction constitutes dicta to the effect that the decision in the *Vallely* case is justified because the attack upon the jurisdiction of the court was made in the same bankruptcy proceeding as the order involved. The language of the United States Supreme Court, however, does not permit the drawing of such an inference because immediately following the sentence heretofore quoted, the court said: "We do not comment upon the significance of this variable." Fairness would have required of appellees not to have omitted this important qualification to the quotation recited by appellees on page 31 of their brief. The United States Supreme Court definitely refused to comment upon the significance of the variance in facts, thus leaving the question open for future considera-

tion. Further decisions do provide us with the answer of the United States Supreme Court on this point. No less than two Supreme Court decisions subsequent to *Stoll v. Gottlieb* have involved attacks made in the *same proceeding* in which the order involved had been made. One of these, *Robert H. Jackson, Atty. Gen. of U. S. v. Irving Trust Co., et al.*, 85 L. Ed. (Adv. Op.) 310, was cited in our opening brief and was referred to by appellees in their answer (Appellees' brief p. 29) and referred to by them merely as an exception to the rule. The other case is that of *Sampsell v. Imperial Paper & Color Corp.*, 85 L. Ed. (Adv. Op.) 797, which was cited in our opening brief and which received no answer whatsoever from appellees. This latter case was a bankruptcy case and the jurisdictional attack upon the order of the bankruptcy court came *within the same bankruptcy proceeding,* and after time to review or appeal had expired. The United States Supreme Court refers to this attack as a *collateral attack* and not as a direct attack. The court says:

> "Furthermore, there was no appeal from the order entered in the summary proceedings. It therefore could not be collaterally attacked in the proceedings by which respondent sought priority for its claim."

Ex parte Sawyer, 124 U. S. 200, 31 L. Ed. 402, 8 S. Ct. 482; *Ex parte Fisk,* 113 U. S. 713, 28 L.Ed. 1117, 5 S. Ct. 724; as well as other cases cited by appellees must be considered in the light of the subsequent cases of the United States Supreme Court, such as *Stoll v. Gottlieb, supra; Chicot County Drainage Dist. v. Baxter State Bank,* 308 U. S. 371, 60 S. Ct. 317, 84 L. Ed. 329 (rehearing denied, 309 U. S. 695, 60 S. Ct. 581, 84 L. Ed. 1035); *Treinies v. Sunshine Mining Co.,* 308 U. S. 66; *Sunshine Anthracite*

Coal Co. v. Adkins, 310 U. S. 381, 84 L. Ed. 1263, 60 S. Ct. 907, 84 L. Ed. 1276; *Robert Jackson v. Irving Trust Co., et al., supra;* and *Sampsell v. Imperial Paper & Color Corp., supra.* The *Ex parte Sawyer* case was not without the vigorous dissenting opinions of Mr. Chief Justice Waite and Mr. Justice Harlan which pointed the way to the majority opinion in *Stoll v. Gottlieb* and subsequent cases.

Appellees' contention that an attack upon the jurisdiction of the court in making an original order from which a contempt proceeding arises is a direct rather than a collateral attack, not only is made by appellees without support of any authority, but comes in the face of direct contradiction of express authority. No less than the United States Supreme Court, in the case of *Oriel v. Russell, et al.,* 278 U. S. 358, 73 L. Ed. 419, 49 S. Ct. 173, holds that a turnover order cannot be collaterally attacked on a motion for commitment for contempt. In this case the contempt proceeding took place in the *same* bankruptcy proceeding wherein the turnover order was made. The time for appeal having expired, the attack upon such order was not a direct one but a collateral one. The late Chief Justice Taft, in writing the opinion of the court, said:

> "The referee and the court, in passing on the issue under such a turnover motion, should, therefore, require clear evidence of the justice of such an order before it is made. Being made, it should be given weight in the future proceedings as one that may not be *collaterally attacked* by an effort to try over the issue already held and decided at the turnover. Thereafter on the motion for commitment the only evidence that can be considered is the evidence of something that has

> happened since the turnover order was made showing that since that time there has newly arisen an inability on the part of the bankrupt to comply with the turnover order." (Italics ours.)

We are cognizant of the fact that the case of *Beauchamp v. U. S., supra,* cited by appellees, appears to permit an attack upon the jurisdiction of the court to issue the order the violation of which is the basis of the contempt proceedings at any time including the contempt proceeding.

The *Beauchamp* case was decided by this Honorable Court before *Stoll v. Gottlieb* and before the United States Supreme Court had definitely determined the sanctity of the court's own determination as to its own jurisdiction. The *Beauchamp* case can now be reconciled on the special concurring opinion of Circuit Justice Wilbur, who pointed out that the contempt proceeding itself was defective because the allegations were insufficient to tie up the alleged contemnor with the violation of the injunction. Judge Wilbur agreed that the injunction had been erroneously granted by the referee but declared that it was too late to raise such a defense. His Honor said:

> "I also agree that the injunction was erroneously granted, but such error is not a defense to a charge of contempt for violating the order. The remedy is by an appeal from the order granting the injunction. The court issuing the injunction had jurisdiction over the parties enjoined and over the subject enjoined and over the subject matter and the order was not void."

We believe that the law has been very ably set forth in a recent decision of the Circuit Court of Appeals for the Second Circuit, in the case of *U. S. v. Jaeger,* 117 Fed. (2d) 483. In this decision (opinion by Justice Clark) the court said:

> "Nevertheless it appears on the authorities that, however harsh may be the result as to the relator herein, that issue is not open to collateral attack. What we have said indicates that in an appropriate case the bankruptcy court could have made the order in question. It is now well settled that on contempt proceedings no attack can be made on the regularity, correctness, or validity of the original order. *Oriel v. Russell,* 278 U. S. 358, 49 S. Ct. 173, 73 L. Ed. 419, affirming *In re Oriel,* 2 Cir., 23 F. 2nd 409, 413; *In re Siegler,* 2 Cir., 31 F. 2nd 972; *In re Arctic Leather Garment Co., supra; Id.,* 2 Cir., 106 F. 2nd 99; cases collected 3 Moore's Collier on Bankruptcy, 14th Ed., 535-537. A like rule applies to *habeas corpus* proceedings; they cannot be used to review, as on appeal, the court action which has led to the commitment order. *Craig v. Hecht,* 263 U. S. 255, 44 S. Ct. 103, 68 L. Ed. 293, affirming *Ex parte Craig,* 2 Cir., 282 F. 138; *Ex parte Kearney,* 7 Wheat. 38, 20 U. S. 38, 5 L. Ed. 391; *United States ex rel. Paleais v. Moore,* 2 Cir., 294 F. 852.
>
> Relator has appealed from neither the commitment nor the contempt order; he therefore can raise here the issue of jurisdiction only. Yet he had opportunity to and did raise that issue in the prior proceedings,

and the court found against him. Even if we assume that the court was acting upon erroneous grounds as indicated above, yet *Stoll v. Gottlieb,* 305 U. S. 165, 59 S. Ct. 134, 83 L. Ed. 104, makes it clear that the matter is settled against *collateral attack.* There the issue whether or not the bankruptcy court could release a guarantor in reorganization from his guaranty was decided by the Court in favor of its jurisdiction. Yet the Supreme Court holds that, even if that ruling be erroneous, and the matter without the power of a bankruptcy court (*In re Diversey Bldg. Corp.,* 7 Cir., 86 F. 2nd 456; *In re Nine North Church Street, Inc.,* 2 Cir., 82 F. 2nd 186), the issue cannot be raised collaterally. The situation seems the same as that here presented. Later decisions of the Court reiterate and reinforce this conclusion. *Jackson v. Irving Trust Co.,* Jan. 6, 1941, 61 S. Ct. 326, 85 L. Ed. .....; *Chicot County Drainage Dist. v. Baxter State Bank,* 308 U. S. 371, 378, 60 S. Ct. 317, 84 L. Ed. 329; cf. 40 Col. L. Rev. 1006, 1008; 53 Harv. L. Rev. 652, 659; 49 Yale L. J. 959; and see also *Ripperger v. A. C. Allyn & Co.,* 2 Cir., 113 F. 2nd 332, certiorari denied 61 S. Ct. 136, 85 L. Ed. .....; *Commercial Cable Staffs' Assn. v. Lehman,* 2 Cir., 107 F. 2nd 917, 921."

In the light of this case it is obvious that the jurisdictional question having been raised by appellees before the referee, the contempt proceeding is a subsequent proceeding and a collateral attack on the jurisdictional question can no longer be heard.

The Stipulation to the Entry of the Order of Injunction Was a Consent to the Jurisdiction of the Court.

Appellees argue that the stipulation to the entry of the order of injunction is not grounds for holding the District Court in error for permitting an attack upon the jurisdiction of the court and dismissing the contempt proceedings. Appellees argue that the stipulation was made with the reservation of objection to the jurisdiction of the court. In our opening brief, we pointed out by authorities which have not been refuted by appellees that the stipulation to a judgment is a consent to jurisdiction. Once one has submitted himself to the jurisdiction of the court, it is impossible to retract that consent. In the proceeding which led up to the injunction, the proceedings were terminated because of the voluntary consent, in fact proposal by appellees, that an injunction be stipulated to. Thus, appellees submitted themselves to the jurisdiction of the court. The subsequent attempt to reserve the question of jurisdiction was ineffectual. If a party litigant

> "takes any step consistent with the hypothesis that the court has jurisdiction of the cause and the person, the special appearance is thereby converted into a general appearance irrespective of whether or not it is by its terms limited to a special purpose, *and an attempted reservation of the special appearance and rights thereunder is wholly ineffectual.* * * *" (Italics ours.)
>
> 6 *Cor. Jur.* §1, (c), p. 9.

> "An offer to confess judgment constitutes a general appearance and waives objection to jurisdiction of the person."
>
> *Feldman Investment Co. v. Connecticut, etc.,* 78 Fed. (2d) 838.

In addition to the authorities cited in our opening brief, a recent California decision illustrates the sanctity with which the courts regard stipulations in open court. In *Cathcart v. Gregory*, 45 A. C. A. 252, at page 259, the court said:

> "In *Webster v. Webster, supra* (216 Cal. 485, 14 P. (2d) 522) the Supreme Court said: 'Such a stipulation made in open court constitutes "not only an agreement between the parties but also between them and the court, which the latter is bound to enforce, not only for the benefit of those interested, but for the protection of its own honor and dignity."' "

Reply to Supplementary Brief of Appellees William H. Cree, H. H. McVicar, C. M. Rood and M. M. McCallen Corporation.

The additional argument of appellees Cree, McVicar, Rood and McCallen Corporation in their supplementary brief can be summarized as follows:

That the injunction was against the Bolsa Chica Oil Corporation, its servants, agents and employees only, and that as vendees of the Bolsa Chica Oil Corporation, these appellees are not subject to the injunction and therefore are not in contempt in violating the same. The theory upon which these appellees were brought into the picture was that they, with full knowledge of the injunction, aided and abetted in its violation. One who is not named or referred to in an injunction may nevertheless be guilty of contempt for its violation when such party conspires with others or aids or abets others in violating such injunction. 12 Am. Jur. sec. 26, page 407.

Where an injunction operates *in rem* against specific property or against an illegal use of such property, the

decree is a limitation upon the use of the property, of which all subsequent owners, lessees or occupants must take notice. 12 Am. Jur. sec. 27, page 409.

Any interference with property in the custody of the law whether there had been an injunction or not, constitutes contempt. 12 Am. Jur. sec. 22, page 404.

Of particular significance is the admission in the brief of appellees Bolsa Chica Oil Corporation *et al.,* on page 6, that the well was sold to the McCallen Corporation "rather than violate the injunction". This is not the proper occasion to go into a discussion of the facts. Appellees Cree *et al.* complain that they have not had their day in court (Appellees Brief page 6) These appellees will have their day in court at such time as the case is sent back to the District Court to hear the evidence. The evidence will determine whether or not these appellees conspired with the other appellees in violating the injunction and whether or not they aided or abetted in the violation of the injunction. As previously pointed out, the certificate of contempt of the referee in bankruptcy is presumptively correct. The referee in bankruptcy having been the only tribunal to hear evidence, the contemptuous conduct of these appellees is sustained by the referee's findings.

CONCLUSION.

We respectfully urge that the decision of the lower court, if permitted to stand, would have the effect of crippling the administration of bankruptcy estates by courts of bankruptcy. The decision of the District Court denies to the bankruptcy court the power to enjoin a threatened trespass upon property in its custody.

Furthermore, the decision of the District Court lends judicial approval to an anomalous submission to the

jurisdiction of the court. In other words, the decision of the District Court permits a party litigant to be both in and out of court to his own advantage. Appellees could have refused to have submitted themselves to the jurisdiction of the referee in bankruptcy by not appearing in the proceeding at all. Instead of that they elected to appear, to litigate the question of the court's jurisdiction, to consent to a stipulated order, and to permit such order to become final and binding. The United States Supreme Court has upheld the power of a court of record to determine for itself whether or not it has jurisdiction in a particular case and that determination itself is *res judicada* if permitted to become final. It follows therefore that appellees having permitted the injunctive order of the referee in bankruptcy which overrules appellees' jurisdictional objections to become final, cannot now challenge that order collaterally, after they decide to violate it.

The record reveals that appellees had ample notice of the harm that would be done to appellant's oil well by the use of mud as a circulating medium in the drilling of their own well. This knowledge was brought to them by the experience suffered as a result of the "Termo" well and by the engineering and geological testimony presented before the referee as to the threat to appellant's property involved in appellee's proposed use of mud. To use a colloquialism, the shameless violation of the injunctive order became the "proof of the pudding", in view of the fact that irreparable damage was incurred by appellant's well as a result of such misconduct by appellees.

For which reasons appellant respectfully urges the reversal of the decision of the District Court.

Respectfully submitted,

JOSEPH J. RIFKIND and
RAPHAEL DECHTER,

By RAPHAEL DECHTER,

Attorneys for Appellant.

No. 9790

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE T. GOGGIN, Trustee in Bankruptcy of the Estate of Jack Dave Sterling, Bankrupt,

Appellant,

vs.

BOLSA CHICA OIL CORPORATION, a Corporation, THOS. W. SIMMONS, ALLAN A. ANDERSON, WILLIAM H. CREE, H. H. McVICAR, C. M. ROOD, and M. M. McCALLEN CORPORATION, a Corporation,

Appellees.

SUPPLEMENTARY BRIEF OF APPELLEES WILLIAM H. CREE, H. H. McVICAR, C. M. ROOD AND M. M. McCALLEN CORPORATION, A CORPORATION.

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SUPPLEMENTARY BRIEF OF APPELLEES.

Opening Statement.

Appellees M. M. McCallen Corporation, a corporation, H. H. McVicar, C. M. Rood and William H. Cree wish to adopt, in so far as it is applicable to them and their position, the brief already filed herein by appellees Bolsa Chica Oil Corporation, Simmons and Anderson. It will serve no purpose and will cumber the Court to go into the questions and argument of the matter which has been so ably covered in that brief. However, these appellees are

in an entirely different position, as a matter of law than the others; they are even farther from the jurisdiction of the Bankruptcy Court. For the sake of making the situation graphic, and at the risk of repeating briefly some facts already contained in the record so far, these appellees submit the following statement of facts:

Statement of Facts.

The Court is well acquainted with the situation which lead up to and immediatly followed the entry of the injunction order in the Referee's Court. Two phrases in that injunction are of particular importance to these appellees. The injunction was addressed to and against "The Bolsa Chica Oil Corporation, its superintendents, agents and employees". [Tr. p. 30.] The injunction prohibited the use of "circulating fluid used in drilling, redrilling or side-tracking of said Petroleum Well." [Tr. p. 31.] This injunction was dated May 15, 1940. [Tr. p. 32.] The alleged damage to the well of the bankrupt estate, due as they claim to mudding up, occurred on June 8, 1940. [Tr. p. 179.] At that time the well was under the management and control and was owned by Bolsa Chica Corporation. The well was transferred to McCallen Corporation by an Assignment of Oil and Gas Lease [Tr. p. 212], and Drilling and Operating Agreement [Tr. p. 202], under date of August 14, 1940. Subsequent to that time, there is no evidence that McCallen Corporation, or any of these appellees conducted any drilling, redrilling or side-tracking operations in the hole at any time. On the contrary, the

evidence shows that the hole was filled with fractured shale body and that it was impossible to penetrate any deeper than 4200 feet. [Tr. p. 233.] This is well above the oil sand and at a point where the testimony shows the appellants had not objected to the use of mud as a circulating fluid. [Tr. pp. 225 and 226.]

These appellees were not parties to the original hearing in which the Trustee asked for instructions and in which the injunctive order was finally entered. They had no opportunity to be heard at that time. They never stipulated or consented to the making or entering of any order against themselves. They appeared, for the first time, in response to the order to show cause on the petition to have Bolsa Chica and themselves certified for contempt issued against them on August 22, 1940, specially and only for the purpose of objecting to the jurisdiction of the Court to hear or determine the matter. [Tr. pp. 164 and 165.] The Court overruled their objection to the jurisdiction but reserved it to be renewed at the conclusion of the evidence. [Tr. p. 178.] The objection was renewed at that time.

The questions involved in this appeal are supplementary to the questions discussed by the other appellees, and are of importance only if the Court finds against Bolsa Chica Oil Corporation, on all points urged in their brief.

Questions Supplementary to Appellee Bolsa Chica Oil Corporation's Brief.

I.

If the Court finds that the injunction was properly issued within the jurisdiction of the bankruptcy court, against Bolsa Chica Oil Corporation, its superintendent, agents and employees, and that said injunctive order had become final, and was not subject to attack in the contempt proceeding, was that injunction valid and subsisting as against a vendee of Bolsa Chica Oil Corporation, a vendee not being a party named or referred to in the injunction?

II.

If such a vendee is bound by such an injunction, can he be held liable for damages arising from acts committed more than two months before he acquires any interest in the property? As a corollary, can such a vendee be liable in a contempt proceeding when he has not done any of the acts prohibited by the injunction?

III.

(a) Where an attorney acquires information in representing one client of the existence of an injunctive order, is he under any obligation to disclose that information to another client, unrelated to the action and not included in the terms of the injunction?

(b) If he is so obligated, may he and his second clients be held liable for violation of the terms of the injunction as aiders and abettors because of the attorney's representation of both clients?

ARGUMENT.

I.

If the Court Finds That the Injunction Was Properly Issued Within the Jurisdiction of the Bankruptcy Court, Against Bolsa Chica Oil Corporation, Its Superintendent, Agents and Employees, and That Said Injunctive Order Had Become Final, and Was Not Subject to Attack in the Contempt Proceeding, Was That Injunction Valid and Subsisting as Against a Vendee of Bolsa Chica Oil Corporation, a Vendee Not Being a Party Named or Referred to in the Injunction?

For the sake of clarity may we designate Bolsa Chica Corporation, Mr. Simmons and Mr. Anderson as the First Appellees and McCallen Corporation, Mr. McVicar, Mr. Rood and Mr. Cree as Second Appellees. First Appellees' brief, we feel, demonstrates that the Court had no jurisdiction to enter the injunction order which is the basis of this contempt proceeding, and that consequently that injunctive order is void and of no effect upon any of the appellees. If the Court disagrees with us, the Second Appellees on this point, may we respectfully submit the following arguments on our own behalf.

Second Appellees were not parties to the injunction proceeding. [Tr. pp. 27 and 29, *et seq.*] They did not acquire title to the property until long after all damage was done and there is no evidence in the record which shows that Second Appellees at any time "drilled, redrilled or side-tracked". The injunction was dated May 15, 1940. [Tr. p. 32.] The damage was done June 8, 1940. [Tr. p. 179.] The transfer to the McCallen corporation was by a usual form of assignment of oil and gas lease and drill-

ing and operating agreement, both dated August 14, 1940. [Tr. pp. 202 and 212.] The first notice to the McCallen Corporation of the injunction was by letter under date of August 21, 1940. [Tr. p. 214.] Second Appellees therefore have never had their day in Court. They have never had an opportunity to be heard as to the merits of their situation. When they were hailed into Court on this contempt citation [Tr. p. 39], they appeared specially only for the single purpose of objecting to the jurisdiction of the Court [Tr. pp. 174 and 175], which objection was overruled with the right reserved to the appellees to renew the objection at the close of the evidence. The objection was then renewed.

It is elementary that a party cannot be divested of rights without a day in Court. It is equally elementary that an injunction cannot be broader than its terms. This injunction made no effort to bind successsors in interest of the Bolsa Chica Oil Corporation. Its terms made it applicable to Bolsa Chica Oil Corporation, its superintendent, agents and employees and their was no mention of vendees, assignees or successors in interest.

An injunction operates *in personam.*

32 *Cor. Jur.* 83;

Scott v. McDonald, 165 U. S. 107, 17 S. Ct. 262, 41 L. Ed. 648;

Taylor v. S. P. Co., 122 Fed. 147.

A person must be a party respondent or defendant or be expressly named in the injunction to be bound thereby. Mere knowledge that an injunction has been issued and

exists is not enough. There must be some definite connecting link between the parties involved.

Gompers v. Stove Co., 221 U. S. 418;
Garrigan v. U. S., 163 Fed. 16;
Kirby v. Society, 95 Cal. App. 757, 273 Pac. 609;
Cohan v. Shibley, 289 Pac. 169.

In the case of *Berger v. Superior Court,* 175 Cal. 719, 167 Pac. 143, 15 A. L. R. 373, an injunction was issued restraining certain parties and organizations, "their officers, members, agents, clerks, attorneys and servants" from picketing a theatre. Berger was not a party to the action and no relation between himself and any of the parties named was shown. He picketed the theatre and during the time he was thus picketing he was served with a copy of the injunction, but continued his activities. In discussing the matter and reversing the trial court, the Court said as follows:

> "The judgment of contempt was based solely on the fact that he did the specified thing, with actual notice that other persons were enjoined from doing the same thing by a judgment in a civil action to which he was not a party and which did not by its terms prohibit him from doing anything."

In discussing the fact that he had actual notice of the injunction, the Court said:

> "But despite expressions in some authorities that at first blush lend support to the contention of respondent, it is generally held that a theory of disobedience of the injunction cannot be predicated on the act of a person not in any way included in its terms or acting in concert with the enjoined party in support of

his claims. Rigas v. Livingston, 178 N. Y. 20, 70 N. E. 107."

The most significant case on this question is that of *Alemite Mfg. Co. v. Staff,* 42 Fed. (2d) 832. The plaintiff sued Joseph Staff, Louis, John and Samuel Staff. John swore that the business was his alone and a dismissal was entered as to Joseph and Louis. Samuel was never served. A decree was entered in the action against John, "his agents, employees, associates and confederates". At that time Joseph was a salesman for John, but he later quit and started in business for himself. It was proved that, in this new business, he infringed the very patent which had been the subject of the injunction. Proceedings to punish for contempt were brought in the original suit. In passing on this point the Court said:

> "We agree that a person who knowingly assists a defendant in violating an injunction subjects himself to civil as well as criminal proceedings for contempt. This is well settled law. *Ex Parte* Lennon, 166 U. S. 548, 17 S. Ct. 65, 41 L. Ed. 1110; Conkey v. Russell, 111 Fed. 417; Wellesley v. Mornington, 1 Ch. 545. On the other hand no court can make a decree which will bind anyone but a party; a court of equity is as much so limited as a court of law; it cannot lawfully enjoin the world at large, no matter how broadly it words its decree. If it assumes to do so, the decree is *pro tanto brutum fulmen,* and the persons enjoined are free to ignore it. It is not vested with sovereign powers to declare conduct unlawful, its jurisdiction is limited to those over whom it gets personal service, and who therefore can have their day in Court."

In conclusion on this point, then, if the injunction as issued was valid, Second Appellees were not affected or bound by it.

II.

If Such a Vendee Is Bound by Such an Injunction, Can He Be Held Liable for Damages Arising From Acts Committed More Than Two Months Before He Acquires Any Interest in the Property? As a Corollary, Can Such a Vendee Be Liable in a Contempt Proceeding When He Has Not Done Any of the Acts Prohibited by the Injunction?

Second Appellees never violated the injunction in any way. There is not the slightest evidence that they undertook any "drilling, redrilling or side-tracking", or that they used mud as a circulating liquid within 200 feet above the oil sands. [Tr. p. 233.] In fact there is no evidence that the injunction as such was violated at any time *subsequent* to June 8, 1940, if at all. This was a period of two months *prior* to the date that Second Appellees acquired title. How conceivably they could be made responsible for the damage, if any, which was sustained on June 8, 1940, we are at a loss to see.

III.

(a) Where an Attorney Acquires Information in Representing One Client of the Existence of an Injunctive Order, Is He Under Any Obligation to Disclose That Information to Another Client, Unrelated to the Action and Not Included in the Terms of the Injunction?

(b) If He Is So Obligated, May He and His Second Clients Be Held Liable for Violation of the Terms of the Injunction as Aiders and Abettors Because of the Attorney's Representation of Both Clients?

Since Second Appellees were not named in the injunction, were not parties to the action in which it was issued, and have never had a day in Court on the matter, the only conceivable theory upon which they might be susceptible to liability would be that they aided and abetted Bolsa Chica in a fraudulent scheme to violate the injunction by subterfuge. If that is appellant's theory in seeking to impose liability on the Second Appellees, they have fallen dismally short of proving their case. The only evidence in the record which shows any connection between first and second appellees, other than the dubious honor of having been hailed into Court together on the contempt citation, is the fact that during a minor portion of the negotiations after the injunction was issued, William H. Cree represented Bolsa Chica Oil Corporation, as one of its attorneys. He also represents, and has for many years past, McCallen Corporation, McVicar and Rood. It is a fundamental principle of an attorney's code of ethics that all information he acquires from any client is confidential. He is under no duty to disclose any information he acquires from one client to any other client, whether that information is of a personal nature or whether it is a matter of

public record. During his limited representation of Bolsa Chica, Mr. Cree stated that he believed the injunction was invalid and that if he were advising Bolsa Chica what to do, he would tell them to proceed with their drilling operations. Several weeks later the well was sold to his client, McCallen Corporation, but no evidence was offered to show he had any connection with the negotiations for that sale, except for drawing the instruments after the deal had been made. This is the only evidence in the record of a direct or indirect connection between First and Second Appellees. We submit that Mr. Cree was under no obligation to disclose the existence of the injunction to McCallen Corporation, McVicar and Rood. In fact we will go further and state that if he had done so, he would have violated the confidential nature of his relations to his client.

In the matter of *Slater v. Merritt,* 75 N. Y. 268, an injunction was issued restraining a defendant, his attorneys, agents, servants and assistants from entering a certain farm. Thereafter two married daughters of the defendant and his mother occupied the premises. The mother and one of the daughters had been advised by the defendant's attorney to get and keep possession, if they could, he of course knowing of the injunction and being embraced within its terms. The trial court found the defendant and his attorney guilty of contempt. On appeal the appellate court held: first, that before parties can be punished by fine or imprisonment, there must be proof against them tending to show illegal actions; and second, that the above observation applies still more strongly to the case of the attorney. The Court said:

> "Indeed, it can hardly be pretended that there is any evidence against him of counseling or abetting the violation of the injunction unless his admitted advice

to the grandmother to get possession if she could, as dowress, and his advice to the sister to keep possession under her mortgage is claimed to be such. But this court has recently held in People v. Randall, 73 N. Y. 416, that *where an attorney has two clients, one of whom is enjoined and the other, in an independent position is not enjoined, such attorney cannot ordinarily be charged with violation of the injunction in advising or acting professionally for the latter.* He is enjoined as an attorney for the *defendant merely,* and this cannot limit or restrain his professional action in behalf of others." (Italics ours.)

To the same effect is the case of *In re Watts & Sachs,* 190 U. S. 1, 47 Law Ed. 933, 10 A. B. R.

Furthermore a contempt proceeding against an aider and abettor is by nature a criminal proceeding. It is not remedial, but is for the purpose of punishing the wrong doer for contempt. As in all criminal proceedings, the guilt must be established beyond a reasonable doubt and the punishment is by imprisonment and not in civil damages.

32 *Corpus Juris,* 502-3;
Garrigan v. U. S., 163 Fed. 16, 89 C. C. A. 494;
Berger v. Ct., supra.

There is scarcely any evidence here of any relation between the parties, except as vendor and vendee. There is certainly nothing that would indicate that Second Appellees aided and abetted First Appellees in a scheme to evade an injunction order.

In conclusion, Second Appellees, submit that they have never had their day in Court. They are charged with violation of an injunction to which they were not parties, and in which they were not named. There can be no contention that they consented to the entry of the injunction or that they waived their objection to the jurisdicion of the Bankruptcy Court to hear and determine the controversy as to them. They have been cited for contempt of an injunction which they have not in any way violated, they have not "drilled, redrilled or side-tracked" or used "mud as a circulating fluid" in any of these operations. An attempt is being made to force upon them the onus of an injunction, questionable at best, with which their only connection is that they were represented by the same attorney, who for a short period represented one of the parties named in the injunction.

Respectfully submitted,

CREE & BROOKS, and
ELIZABETH R. HENSEL,
By ELIZABETH R. HENSEL,

Attorneys for Appellees M. M. McCallen Corporation, H. H. McVicar, C. M. Rood and William H. Cree.

No. 9826

United States

Circuit Court of Appeals

For the Ninth Circuit.

GIN SOON GING,

Appellant,

vs.

WILLIAM A. CARMICHAEL, District Director of Immigration and Naturalization Service,

Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

No. 9826

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

NAMES AND ADDRESSES OF ATTORNEYS

For Appellant:

YOU CHUNG HONG, Esq.,
445 Ginling Way,
Los Angeles, California.

For Appellee:

WILLIAM FLEET PALMER, Esq.,
United States Attorney,
ATTILIO DI GIROLAMO, Esq.,
Assistant United States Attorney,
600 Post Office and Court House Building,
Los Angeles, California. [1*]

*Page numbering appearing at foot of page of original certified Transcript of Record.

In the United States District Court in and for the Southern District of California
Central Division

No. 14531 M

In the Matter of the Application of
GIN SOON GING
For a Writ of Habeas Corpus

PETITION FOR WRIT OF HABEAS CORPUS

To the Honorable Judge in the above-entitled Court, Your Petitioner, Gin Ting, Respectfully States:

I.

That he was born in the United States and that under the Constitution thereof, he is a citizen of the United States; that as evidence of his said American citizenship, he holds United States Citizen's Certificate of Identity No. 5888 issued to him by the Commissioner of Immigration and Naturalization at San Francisco, California, on November 7, 1911; and that he has never expatriated himself as such a citizen;

II.

That he has a son by the name of Gin Soon Ging born to him and his wife in China on May 25, 1926, and that under the provisions of Section 1993 of the Revised Statutes, the said Gin Soon Ging is also a citizen of the United States; and that on or about June 30, 1940, his said son came to the port

of San Pedro, California and applied to the Immigration and Naturalization Authorities thereof for admission so as to join the petitioner in this country;

III.

That on July 9, 1940, a board of special inquiry was convened to hear the application of the aforesaid Gin Soon Ging for admission to the United States as a natural born citizen thereof; that your petitioner and his clansman Gin Wing Fun appeared [2] before the said board as witnesses in the applicant's behalf; that after hearing the testimony concerning the applicant's ancestors, parents, brothers, and other relatives, his family home, ancestral village and schooling in China, and many other collateral matters pertaining to the applicant's claimed relationship to your petitioner, the board of special inquiry denied the said application, not because of any inconsistencies in the testimony between your petitioner and the said Gin Soon Ging but because of certain discrepancies between your petitioner and his older son Gin Hong Goon in certain proceedings which took place in 1931 and 1937 to which the present applicant Gin Soon Ging was not a party;

IV.

That the board of special inquiry upon receipt of an anonymous letter to the effect that the applicant was your petitioner's grandson instead of his son, reopened the hearing on July 23, 1940 in

order to question the parties hereto along the line of the information so anonymously received; and that at the conclusion of this supplementary hearing, the applicant was again excluded;

V.

That an appeal from the excluding decision by the board of special inquiry was forthwith taken to the Board of Review of the Attorney-General, but the appellate board on September 24th, 1940 dismissed the appeal and instructed the District Director of Immigration and Naturalization for the port of San Pedro, California to deport the said Gin Soon Ging on the first available steamer leaving for China; that unless this Honorable Court intervene, Gin Soon Ging will be promptly taken out of the United States; and that the aforesaid proceedings involved a question of citizenship and denial of a fair hearing to an American citizen, over which this Honorable Court has undisputed jurisdiction,—Wong Hai Sing vs. Nagle, C. C. A. 9, 49 Fed. (2d) 1016; and,

VI.

That the evidence adduced before the Immigration Authorities [3] established to a reasonable certainty that the applicant Gin Soon Ging is the son of your petitioner in that there was not a single discrepancy in the testimony concerning the applicant's family history, relatives, home life, ancestral

village, and schooling, the movements of various members of applicant's father's family, important events as well as collateral matters which were commonly known to members of this family; that it was arbitrary and unfair for the Immigration Authorities to exclude the applicant where the evidence submitted has so conclusively established the relationship of father and son between your petitioner and the said Gin Soon Ging—Jue Yim Ton vs. Nagle, C. C. A. 9, 48 Fed. (2d) 752; that the immigration tribunals may ascertain facts in any reasonable and fair way they see fit, but they cannot reject sworn, consistent, unimpeached and uncontradicted testimony without real reason which fair-minded persons would regard as adequate—Ward vs. Flynn ex rel Yee Gim Lung, 74 Fed. (2d) 145; that the discrepancies developed in the hearings of Gin Hong Goon in 1931 and 1937 to which the present applicant Gin Soon Ging was not a party, utilized by the Immigration Authorities to exclude the applicant conclusively showed unfairness and prejudice—Flynn ex rel Chin King vs. Tillinghast, 32 Fed. (2d) 359; Ex parte Ng Bin Fon, 20 Fed. (2d) 1014; and U. S. ex rel Fong Lung Sing vs. Day, 29 Fed. (2d) 619; and, that it was unfair and a violation of the due process of law for the Immigration Authorities to base an excluding decision on mere suspicion brought about by an anonymous letter—Wong Gook Chun vs. Proctor, C. C. A. 9, 84 Fed. (2d) 763.

VII.

Your petitioner further states that the said Gin Soon Ging has been since July 9th, 1940 and is now being held in detention at the Immigration Station at San Pedro, California in the custody of [4] William A. Carmichael, District Director of Immigration and Naturalization, for which reason, the said Gin Soon Ging is unable to verify this petition, so your petitioner as his father therefore verifies this petition in his behalf.

Wherefore your petitioner prays that a writ of habeas corpus be issued and directed to the aforesaid District Director of Immigration and Naturalization as respondent herein, commanding him to hold the body of the said Gin Soon Ging within the jurisdiction of this Honorable Court and to present the said body before this Court at a time and place to be specified in the said order, together with the time and cause of his detention, so that the same may be inquired into to the end that the said Gin Soon Ging may be restored to his liberty and go hence without day.

Dated at Los Angeles, California, this 25th day of September, 1940.

Y. C. HONG,

Attorney for Petitioner.

State of California,
County of Los Angeles—ss.

Gin Ting, being duly sworn, deposes and states: That he is the petitioner named in the foregoing petition; that the same has been read and explained to him and that he knows the contents thereof which is true of his own knowledge except those matters which are therein stated on information and belief, and as to such matters, he believes the same to be true.

GIN TING,
Petitioner.

Subscribed and Sworn to before me this 25th day of September, 1940.

[Seal] Y. C. HONG,
Notary Public.
Los Angeles, California
September ....., 1940. [5]

Let the writ issue as prayed for returnable before United States District Judge Paul J. McCormick on the 7th day of October 1940 at 2 o'clock in the afternoon.

PAUL J. McCORMICK,
United States District Judge.

Dated Sept. 25, 1940 at 2:10 P. M.

[Endorsed]: Filed Sep. 25, 1940. R. S. Zimmerman, Clerk. By P. D. Hooser, Deputy. [6]

United States District Court
Central Division, Southern District of California

[Title of Cause.]

HABEAS CORPUS

The President of the United States of America
To William A. Carmichael, District Director of Immigration and Naturalization, Los Angeles, California—Greeting:

You Are Hereby Commanded, that the body of Gin Soon Ging, by you restrained of his liberty, as it is said detained by whatsoever names the said Gin Soon Ging may be detained, together with the day and cause of being taken and detained, you have before the Honorable Paul J. McCormick, Judge of the United States District Court in and for the Southern District of California, at the court room of said Court, in the City of Los Angeles at 2:00 o'clock p. m., on the 7th day of October, 1940, then and there to do, submit to and receive whatsoever the said Judge shall then and there consider in that behalf; and have you then and there this writ.

Witness the Honorable Paul J. McCormick, United States District Judge at Los Angeles, California, this 25th day of September, A. D. 1940,

[Seal] R. S. ZIMMERMAN,
Clerk.

By GEO. E. RUPERICH,
Deputy Clerk.

[Endorsed]: Filed Oct. 7, 1940. R. S. Zimmerman, Clerk. By B. B. Hansen, Deputy Clerk. [7]

[Title of District Court and Cause.]

RETURN TO WRIT OF HABEAS CORPUS

I, William A. Carmichael, District Director of U. S. Immigration and Naturalization Service, Los Angeles, California District No. 20, Respondent herein, for my Return to Writ of Habeas Corpus issued herein and in compliance with the said Writ of Habeas Corpus, now produce the body of Gin Soon Ging on this 7th day of October, 1940 before this Honorable Court, and for my Return to said Writ deny that I am unlawfully imprisoning and detaining and confining and restraining the liberty of the aforesaid Gin Soon Ging.

For further Return to said Writ, Respondent admits that the said Gin Soon Ging arrived from China at the Port of San Pedro, California the 30th day of June, 1940 on the SS "President Cleveland" and made application for admission into the United States, and certifies that the true cause of said Gin Soon Ging's detention is the finding and order of a duly and regularly constituted Board of Special Inquiry denying him admission into the United States made July 9, 1940, and the order of the Department of Justice, Washington, D. C., made on or about September 24, 1940 confirming the decision of the said Board of Special Inquiry and ordering the return of said Gin Soon Ging to the country whence he came; that Respondent was preparing to return the said Gin Soon Ging to

the country whence he came when this Writ of Habeas Corpus was issued.

For further Return, Respondent makes a part hereof Department of Justice File No. 56040/574, duly certified, containing transcript of the testimony and summary and findings of the Board of Special Inquiry, San Pedro, California and summary and findings of the Board of Immigration Appeals, Washington, D. C.; also certain [8] U. S. Immigration and Naturalization Service records, identified by file numbers: 10508/10558, 25882/4-4, 30348/4-13, 37221/7-27 (San Francisco, California); 7032/2754 (Seattle, Washington); 31160/503 (San Diego, California); 1521/506, 1521/310, 1522/18 (Tucson, Arizona); Exhibits "A" and "B", and a group photograph.

Respectfully submitted,

WILLIAM A. CARMICHAEL,

District Director of U. S. Immigration and Naturalization Service, Los Angeles, California, District No. 20, Respondent.

[Endorsed]: Filed Oct. 7, 1940. R. S. Zimmerman, Clerk. By B. B. Hansen, Deputy Clerk. [9]

[Title of District Court and Cause.]

TRAVERSE TO RETURN

To the Honorable United States District Judge, now presiding in the United States District Court, in and for the Southern District of California, Central Division,

Your Petitioner by way of traverse to the Respondent's Return herein respectfully alleges:

I

That he realleges and incorporates herein each and every allegation contained in his Petition verified the 25th day of September, 1940; and

II

That the denial contained in the said Return is only a conclusion of law and does not show facts sufficient to warrant the restraint, detention, and contemplated deportation of the said Gin Soon Ging by the Respondent;

Wherefore, it is respectfully submitted that the Writ should be sustained and Gin Soon Ging be discharged from the custody of the Respondent.

Dated at Los Angeles, California, this 10th day of October, 1940.

Y. C. HONG
Attorney for Petitioner. [10]

United States of America
State of California
County of Los Angeles—ss.

Gin Ting, Being Duly Sworn, Deposes and States that he is the petitioner in the foregoing traverse; that same has been read and explained to him and that he knows the contents thereof; that the same is true of his own knowledge except as to those matters which are therein stated on his information and belief, and as to those matters, he believes it to be true.

GIN TING
Petitioner.

Subscribed and Sworn to Before Me This 10th day of October, 1940.

[Seal] Y. C. HONG
Notary Public, Los Angeles County

[Endorsed]: Filed Oct. 10, 1940. [11]

At a stated term, to wit: The February Term, A. D. 1941 of the District Court of the United States of America, within and for the Central Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles on Wednesday the 2nd day of April in the year of our Lord one thousand nine hundred and forty-one.

Present:

The Honorable: Campbell E. Beaumont, District Judge.

No. 14531-B Crim.

In the Matter of the Petition of
GIN SOON GING

for a Writ of Habeas Corpus

This matter having heretofore come before the Court and documentary evidence having been submitted and counsel having submitted written briefs and the Court having fully considered the same and being fully advised as to the facts and the law, now denies petition for Writ of Habeas Corpus and dismisses said Writ. [13]

United States District Court
Southern District of California
Central Division

No. 14531-B

In the Matter of
GIN SOON GING

MEMORANDUM AND ORDER

The writ challenges a denial of admission to the United States of Gin Soon Ging, a Chinese boy, who claims to be a son of a native United States citizen. The Board of Special Inquiry held that

the relationship had not been established, and upon appeal its decision was affirmed by the Board of Review.

After a study of the record herein the Court cannot say that the Board of Special Inquiry committed a manifest abuse of the power and discretion conferred upon it. In this case the evidence is such that reasonable men might differ as to its probative effect. It was the Board's duty to determine such effect, and it cannot be said that its decision, which represented the unanimous agreement of its members, was reached unfairly or arbitrarily. In such circumstances its decision will not be disturbed. Lum Sha You v. United States (C. C. A. 9th), 82 Fed. (2d) 83; Quon Quon Poy v. Johnson, 273 U. S. 352; United States v. Ju Toy, 198 U. S. 253; Chin Yow v. United States, 208 U. S. 8; Chin Share Nging v. Nagle, 27 Fed. (2d) 848; Mui Sam Hun v. United States, 78 Fed. (2d) 612.

Petition is denied and the writ discharged. April 1, 1941.

BEAUMONT, J.

[Endorsed]: Filed Apr. 10, 1941. [14]

[Title of District Court and Cause.]

NOTICE OF APPEAL

To the Clerk of the above-entitled Court, to William A. Carmichael, District Director of Immigration and Naturalization, and to William Fleet Palmer, Esq., United States Attorney, Attorney for Respondent:

You and each of you will please take notice that Gin Soon Ging, the applicant in the above-entitled matter, hereby appeals to the United States Circuit (*Court*) of Appeals for the Ninth Circuit, from the Order and Judgment rendered, made and entered herein on April 2, 1941, discharging the writ of habeas corpus.

April 11th, 1941, Los Angeles, California.

Y. C. HONG

Attorney for Petitioner

Received Copy of the Within Notice of Appeal this 11th day of April, 1941.

RUSSELL LAMBEAU,

By MMH

Received Copy of the Within Notice of Appeal this day of April, 1941.

A. DI GIROLAMO,

Asst. U. S. Atty.

Copy mailed to District Director 4/11/41, E. L. S.

[Endorsed]: Filed Apr. 11, 1941. [15]

[Title of District Court and Cause.]

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY AND DESIGNATION OF THE PARTS OF RECORD WHICH APPELLANT THINKS NECESSARY FOR THE CONSIDERATION THEREOF.

Comes now Gin Soon Ging, the Appellant in the above-entitled matter, respectfully stating that he intends to rely upon the following points on which the District Court erred, to-wit:

I

In holding that the Board of Special Inquiry at the port of San Pedro, California, did not commit a manifest abuse of the power and discretion conferred upon it, whereas the minutes of the administrative proceedings showed that the said Board's finding to the effect that the appellant was Gin Ting's inadmissible grandson was only based upon anonymous information instead of substantial evidence;

II

In holding that the hearing accorded by the Board of Special Inquiry at San Pedro, California, was not unfair and arbitrary whereas the record of the administrative proceedings showed that the said Board's dissatisfaction as to the appellant's claim of relationship to his alleged father, Gin Ting, was based solely upon certain discrepancies between his alleged father and alleged brother Gin Hong Goon developed in certain immigration proceedings had in 1931 and 1937 to which the present appellant was

not a party and on a matter which did not concern the appellant or his relationship to his alleged father Gin Ting;

III

In failing to hold that the consistent and unimpeached testimony of the appellant and his alleged father, Gin Ting, and other uncontradicted [16] evidence of record submitted to the Board of Special Inquiry at San Pedro, California, had reasonably established his claimed relationship to his alleged father Gin Ting; and,

IV

In dismissing the writ of habeas corpus after it was affirmatively shown that the Immigration Authorities had manifestly abused its power and discretion, and arbitrarily and unfairly denied to the appellant admission to his own country.

V

Therefore, the appellant deems it necessary to, and does hereby request that all the original immigration files and records heretofore submitted as exhibits before the District Court be made exhibits before the Circuit Court of Appeals for the Ninth Circuit by filing the same with the Clerk of the said appellate court in accordance with the stipulations adopted on April 25, 1941, by and between the parties hereto.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for Appellant

[Endorsed]: Filed Apr. 25, 1941. R. S. Zimmerman, Clerk. By P. D. Hooser, Deputy. [17]

[Title of District Court and Cause.]

STIPULATION AND ORDER REGARDING ORIGINAL RECORDS AND FILES OF THE DEPARTMENT OF JUSTICE.

It is hereby stipulated and agreed by and between Y. C. Hong, Attorney for Appellant herein, and William Fleet Palmer, Attorney for the Appellee herein, that the original files and records of the Department of Justice covering the application of the above-named party, which were files in the hearings in the above-entitled cause, may be by the Clerk of this court sent to the Clerk of the Circuit Court of Appeals for the Ninth Circuit, as part of the appellate record, in order that the said original immigration files may be considered by the Circuit Court of Appeals for the Ninth Circuit in lieu of a certified copy of the said records and files, and that the same need not be printed.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for Appellant
WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney
Attorneys for Appellees

On this 25th day of Apr., 1941.
It is so ordered.

PAUL J. McCORMICK
United States District Judge [18]

[Title of District Court and Cause.]

STIPULATION AND ORDER IN RE PRINTING OF TRANSCRIPT OF RECORD

It is hereby stipulated and agreed by and between the parties to the above-entitled cause, through their respective counsel, that the Clerk of the above-entitled Court, in preparing the printed transcript of record on appeal, may omit the heading of all papers filed except the citation, petition for writ of habeas corpus, and assignments of error, substituting in the place and stead thereof the phrase "Title of Court and Cause", and that the said Clerk may omit all backs of documents except the filing endorsements.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for Appellant
WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney
Attorneys for Appellee

It is so ordered.

Apr. 25th, 1941.

PAUL J. McCORMICK
United States District Judge

[Endorsed]: Filed Apr. 25, 1941. R. S. Zimmerman, Clerk. By P. D. Hooser, Deputy. [19]

[Title of District Court and Cause.]

DESIGNATION OF RECORD ON APPEAL

To the Clerk of the Said Court:

Please prepare and duly authenticate the transcript of the following portions of the record in the above-entitled case for appeal to the United States Circuit Court of Appeals for the Ninth Circuit;

1. Petition for Writ of Habeas Corpus and Order granting writ;
2. Writ of Habeas Corpus;
3. Return to writ of Habeas Corpus;
4. Traverse to Return;

5. Minute and Memorandum and Order of District Court discharging writ;

6. Notice of Appeal;

7. Cost Bond on Appeal;

8. Stipulation and Order Regarding Original Records and Files of the Department of Justice;

9. Stipulation and Order in re Printing of Transcript of Record;

10. Statement of Points on Which Appellant Intends to Rely and Designation of the Parts of Record Which Appellant Thinks Necessary for the Consideration Thereof.

11. Designation of Record on Appeal.

April 25, 1941.

Y. C. HONG
Attorney for Petitioner and Appellant.

Approved:

WM. A. CARMICHAEL H
District Director of Immigration
Respondent-Appellee.

WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney

[Endorsed]: Filed Apr. 25, 1941. R. S. Zimmerman, Clerk, by P. D. Hooser, Deputy. [21]

[Title of District Court and Cause.]

COST BOND ON APPEAL

Know All Men by These Presents:

That the undersigned Fidelity and Deposit Company of Maryland is held and firmly bound unto the United States of America, in the full and just sum of Two Hundred and Fifty Dollars ($250.00), to be paid to the United States of America, or their attorney, successors or assigns, to which payment, well and truly to be made, the undersigned binds himself, his heirs, executors and administrators, jointly and severally by these presents.

Sealed with his seal and dated this 25th day of April, 1941, at Los Angeles, California.

Whereas, lately in a habeas corpus proceeding in the United States District Court for the Southern District of California, Central Division, between the petitioner Gin Soon Ging and the respondent William A. Carmichael, District Director of Immigration and Naturalization with supervision over the port of San Pedro, California, as aforesaid, an order, judgment and decree was rendered by the said Court on the 1st day of April, 1941, against the said Gin Soon Ging, discharging the writ of habeas corpus and remanding the said petitioner to the custody of the respondent for deportation, and the said petitioner Gin Soon Ging thereupon on the 11th day of April, 1941, filed his notice of appeal with the Clerk of the said Court to have the United

States Circuit Court of Appeals for the Ninth Circuit, to review and reverse the said order, judgment and decree in the aforesaid habeas corpus proceeding.

Now, the condition of the above obligation is such that if the said Gin Soon Ging shall prosecute his appeal to effect and answer all costs if [23] he fails to make his plea good, then the above obligation to be void, else to remain in full force and virtue.

FIDELITY AND DEPOSIT
COMPANY OF MARYLAND
By ROBERT HECHT
Attorney in Fact

Attest:
[Seal] S. M. SMITH
Agent

State of California,
County of Los Angeles—ss.

On this 25th day of April, 1941, before me Theresa Fitzgibbons, a Notary Public, in and for the County and State aforesaid, duly commissioned and sworn, personally appeared Robert Hecht and S. M. Smith, known to me to be the persons whose names are subscribed to the foregoing instrument as the Attorney-in-Fact and Agent respectively of the Fidelity and Deposit Company of Maryland, and acknowledged to me that they subscribed the name of Fidelity and Deposit Company thereto as Prin-

cipal and their own names as Attorney-in-Fact and Agent, respectively.

[Seal] THERESA FITZGIBBONS

Notary Public in and for Los Angeles County, State of California.

My Commission Expires May 3, 1942.

[Endorsed]: Filed Apr. 28, 1941. [24]

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, R. S. Zimmerman, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 25 inclusive, contain full, true and correct copies of Petition for Writ of Habeas Corpus; Order for Writ; Writ of Habeas Corpus; Return to the Writ; Traverse to the Return; Minute of Decision; Memorandum and Order Discharging the Writ; Notice of Appeal; Statement of Points on Appeal; Stipulation and Order Re Original Immmigration Records; Stipulation and Order Re Printing; Designation of Record on Appeal; and Cost Bond on Appeal, which together with the Original Records of the Immigration and Naturalization Service transmitted herewith constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I do further certify that the fees of the Clerk for comparing, correcting and certifying the foregoing record amount to $4.70 and that the said amount has been paid to me by the Appellant.

Witness my hand and the seal of the District Court of the United States for the Southern District of California, this 16th day of May, A. D. 1941.

[Seal] R. S. ZIMMERMAN,
Clerk,
By: EDMUND L. SMITH
Deputy.

[Endorsed]: No. 9826. United States Circuit Court of Appeals for the Ninth Circuit. Gin Soon Ging, Appellant, vs. William A. Carmichael, District Director of Immigration and Naturalization Service, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Southern District of California, Central Division.

Filed May 17, 1941.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 9826

GIN SOON GING,

Appellant,

vs.

WM. A. CARMICHAEL, District Director of Immigration and Naturalization,

Appellee.

STATEMENT OF POINTS ON WHICH APPELLANT INTENDS TO RELY ON THE APPEAL AND DESIGNATION OF NECESSARY PARTS OF RECORD FOR THE APPEAL.

STIPULATION

(Rule 19, Subdivision 6 of Circuit Court of Appeals in and for the Ninth Circuit.)

It is hereby stipulated by and between the parties hereto through their respective counsel pursuant to Rule 19, Subdivision 6 of the Rules of the Circuit Court of Appeals in and for the Ninth Circuit, that the Statement of Points and Designation of Parts of Record filed in the District Court on the 25th day of April, 1941, and each and every part thereof, shall be and is hereby designated as necessary for the consideration of the appeal herein.

Dated this 25th day of April, 1941, at Los Angeles, California.

Y. C. HONG
Attorney for the Appellant
WM. FLEET PALMER
United States Attorney
By ATTILIO DI GIROLAMO
Asst. United States Attorney
Attorneys for the Appellee

[Endorsed]: Filed May 17, 1941. Paul P. O'Brien, Clerk.

No. 9826.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GIN SOON GING,

Appellant,

vs.

WM. A. CARMICHAEL, District Director of Immigration and Naturalization,

Appellee.

BRIEF FOR APPELLANT.

YOU CHUNG HONG,
445 Gin Ling Way, Los Angeles,
Attorney for Appellant.

Parker & Baird Company, Law Printers, Los Angeles.

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No. 9826.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GIN SOON GING,

Appellant,

vs.

WM. A. CARMICHAEL, District Director of Immigration and Naturalization,

Appellee.

BRIEF FOR APPELLANT.

Pleadings.

This is an appeal from an order of the District Court dismissing the writ of habeas corpus previously issued upon the application of the appellant. The petition was made by appellant's father, Gin Ting, on September 25th, 1940 [Tr. of R. pp. 2-7], the writ was issued and served on the same day [Tr. of R. p. 8], the appellee's return to the writ attaching the Immigration records involved was filed on October 7, 1940 [Tr. of R. pp. 9-10], and traverse to the return was submitted in the appellant's behalf on October 10th, 1940 [Tr. of R. pp. 11-12]. Issue was thus joined.

Jurisdictional Statement.

Jurisdiction of the court below to review the proceedings of the Immigration Service was invoked by the appellant on the ground that he was denied a fair hearing of his case under the provisions of 28 U. S. C., Section 451

(R. S., Section 751). The present appeal is authorized by the provisions of 28 U. S. C., Section 225-a (Jud. Code, 128, as amended).

Facts of the Case.

Gin Soon Ging, the appellant, was a 14-year-old boy of the Chinese race who came to the port of San Pedro, California on June 30th, 1940 and applied to the Immigration authorities there for admission as a natural born American citizen by virtue of the provisions of Section 1993 of the Revised Statutes. He left China to join his American-born father, Gin Ting, in this country. As evidence of his citizenship, Gin Ting presented United States Citizen's Certificate of Identity No. 5888 issued to him by the Commissioner of Immigration and Naturalization at San Francisco, California on November 7th, 1911. Appellant claimed that he was born to the said Gin Ting and wife on May 25th, 1926 in China, and that he was therefore entitled to admission as the foreign-born son of a native-born American citizen under the aforesaid statute.

Appellant's application was heard by a board of special inquiry on July 9th, 1940. His alleged father, Gin Ting, and clansman, Gin Wing Fun, appeared before the board to testify in his behalf. After hearing the testimony of the appellant and his two witnesses on matters concerning his ancestors, parents, brothers and other relatives, the detailed description of his Chinese home, ancestral village and schooling as well as many other matters and events which the board believed the appellant and his alleged father should have common knowledge by virtue of their relationship to each other, no discrepancies or inconsistent statements were developed. The board nevertheless, denied the appellant the right of admission and based its exclud-

ing decision solely on the ground that there were some discrepancies between the testimony of his alleged father and Gin Hong Goon in certain Immigration proceedings had in 1931 and 1937 to which the appellant was not even a party. The board was also in receipt of an anonymous letter saying that the appellant was Gin Ting's grandson and not his son, so an additional finding to that effect was made for the appellant's exclusion.

Appeal was then taken to the Immigration Board of Review in Washington, D. C., that the hearing was unfair and findings were not supported by facts. The appellate board, however, dismissed the appeal and confirmed the excluding order of the trial board. Thereupon, a writ of habeas corpus was applied for by the appellant's father in his behalf to obtain judicial review of the same. This is an appeal from the order of the court below dismissing the writ.

Specifications of Error.

The court below held that the board of special inquiry did not commit a manifest abuse of the power and discretion conferred upon it and that the excluding decision rendered against the appellant was not reached unfairly or arbitrarily [Tr. of R. pp. 12-14]. Appellant believes the court below was in error. Specifications of error are expressed in his statement of points for appeal filed on April 25th, 1941 [Tr. of R. pp. 16-18].

The question at issue may therefore be succinctly stated as follows: *Was the hearing accorded the appellant by the Immigration Authorities arbitrary and unfair?* Appellant contends that he was denied the fair hearing to which he was entitled.

ARGUMENT.

I.

The Board of Special Inquiry Committed a Manifest Abuse of the Power and Discretion Conferred Upon It by Arbitrarily Rejecting the Uncontradicted Testimony of the Appellant's Alleged Father Concerning His Relationship to the Appellant.

There was not a single discrepancy developed between the testimony of the appellant and his alleged father before the board of special inquiry. The examination accorded them touched upon every detail pertaining to their ancestral history, family, relatives, home, village, and hundreds of various collateral events which took place during their lives. The pedigree reputation was also corroborated by the testimony of their clansman Gin Wing Fun. The board, however, arbitrarily brought into the picture certain discrepancies developed in 1931 and 1937 between the testimony given by the appellant's father and appellant's alleged brother, Gin Hung Goon, who failed to gain admission to this country, and sought thereby to discredit the appellant's father's present testimony.

Of course, the law's method of ascertaining the credibility of witnesses is nothing new and has been known for centuries. Aside from the appearance of the witness, his demeanor on the stand, the reasonableness of his testimony, and his character, he can only be impeached by evidence of contradictory statements made out of court or in another tribunal on material matters. *Gung You v.*

Nagle (C.C.A. 9th), 34 Fed. (2d) 848, 852. The matter material to appellant's case is the relationship between the appellant and his alleged father. Not only was there no disclaimer of such parentage by appellant's father in the 1931 and 1937 proceedings, the official records of those proceedings are replete with antecedent testimony by him concerning the birth and existence of the appellant in his family and home in China. There was, therefore, no valid ground for the board to reject either the present or previous testimony of the appellant's father pertaining to his relationship to the appellant. To do so is an unwarranted abuse of power and discretion.

On appeal to the appellate board in Washington, D. C., the language used in the decision rendered on September 18th, 1940, reads as follows:

> "The Board of Special Inquiry appears to have found the appellant's alleged father to be discredited as a witness by reason of the record fact that in 1931 and again in 1937 he testified in support of the claim of one Gin Hung Quon to be his son and, therefore, entitled to admission as a citizen, which claim was not found to be established with the result that the said Gin Hung Quon was returned to China at the conclusion of those two proceedings. *Reference to the records of those two applications, however, fails to show that fraud was proved or even alleged in either of them. Thus, it is not believed that the Board of Special Inquiry is warranted in finding the alleged father discredited by reason of his testifying in those proceedings.*" (Emphasis ours.)

II.

The Board of Special Inquiry Was Arbitrary and Unfair in Relying on the Questionable Contents of an Anonymous Letter to Base an Order of Exclusion Because the Rights and Privileges of Citizenship Cannot Be So Lightly Denied the Appellant.

Shortly previous to the supplementary hearing held on July 23rd, 1940, the board of special inquiry was in receipt of an anonymous communication to the effect that the appellant was Gin Ting's grandson and not his son as claimed. During the course of the hearing, appellant's father produced a family group photograph taken in China many years ago as additional evidence of relationship which was overlooked in the first hearing and in which appeared the appellant, his mother Lee Shee, his younger brother Gin Soon Pang, his older brother Gin Hung Goon and the latter's wife Wong Shee. After the unexpected introduction of this photograph, the board showed it to the appellant who without any hesitation identified and named each and every person therein. The board, however, paid lip service to the law as laid down by our Supreme Court in *Kwock Jan Fat v. White,* 253 U. S. 454, 40 S. Ct. 566, 64 L. Ed. 1010, by stating that the anonymous information was given "no credence" because of its source, came out with the wild stab in the dark by finding that the said photograph appeared to be that of a "father and mother and two children and a grandmother", which alleged opinion if it were based on fact, would furnish support to the allegation contained in the anonymous letter, and, of course, would make the appellant's mother his grandmother. This remarkable finding of the board may be characterized solely as a prejudicial effort to give full weight and credence to the anonymous infor-

mation whipsawing the evidence around to suit the convenience of the suspicion of the members of the board by making the wish the father to the thought. Even the Immigration Board of Appeals had to acknowledge the invalidity of such a ground on September 18, 1940, as follows:

> "Also, it appears that while the Board of Special Inquiry has given no credence to anonymous information that this appellant is a grandson instead of a son of his alleged father; yet, *that Board appears to have indirectly given some weight to that information in finding that the group photograph presented 'would appear to be the photograph of father and two children and a grandmother', which would accord with the anonymous information,* instead of being, as the alleged father and appellant testify, a picture of the appellant and his mother, and his older brother and the latter's wife, and his younger brother." (Emphasis ours.)

Under the same circumstances, this Honorable Court held in the case of *Chew Hoy Quong v. White* (C.C.A. 9th), 249 Fed. 869, 870, as follows:

> "Aside from that, we hold that the fact that the immigration authorities received a confidential communication concerning the applicant's right to admission, upon which they acted, and which was forwarded to the Department of Labor for its consideration, was *sufficient to constitute the hearing unfair.* However far the hearing on the application of an alien for admission into the United States may depart from what in judicial proceedings is deemed necessary to constitute due process of law, *there clearly is no warrant for basing decision, in whole or in part, on*

confidential communication, the source, motive, or contents of which are not disclosed to the applicant or her counsel, and where no opportunity is afforded them to cross-examine, or to offer testimony in rebuttal thereof, or even to know that such communication has been received." (Emphasis ours.)

See, also:

Wong Gook Chun v. Proctor (C.C.A. 9th), 84 Fed. (2d) 763.

III.

The Board of Special Inquiry Acted Most Arbitrarily and Unfairly by Disregarding Direct and Material Evidence on the Issue of Relationship Between the Appellant and His Alleged Father in Order to Render Its Decision of Exclusion.

By reason of the fact that Gin Ting had not been back to China since 1927 when the appellant was an infant two years old, the board of special inquiry disregarded the testimony in support of the claimed relationship. This Honorable Court in the case of *Gung You v. Nagle,* 34 Fed. (2d) 848, 852, said:

"Relationship is not usually proved by physical facts, and never is where the mother does not testify, but by pedigree reputation in the family, and by the conduct of the parties, including the manner in which they live. The fact that a small child lives in the home of its alleged parents and that they maintain toward each other the obligation involved in the relationship is evidence favorable to the issue, and evi-

dence that they did not live together and did not conduct themselves as parent and child is evidence to the contrary. *Such evidence is not collateral evidence; it is direct and material evidence on the issue.*" (Emphasis ours.)

The mere fact that the appellant's father has not seen the appellant in person since the latter was an infant therefore could not reasonably discredit his father's testimony on his conduct toward the appellant, or testimony of others on the pedigree reputation in their family. In 22 Corpus Juris 172, Section 103 g, the following passage is found, viz.:

"Relationship. The rule admitting declarations concerning pedigree applies to a question of relationship; in addition to which a person may testify as to his relationship to another person, especially where the statement is based on his own knowledge; and parentage may be proved by general reputation."

And in 22 Corpus Juris 173, Section 106 (3), the following is noted:

"Identity. In the absence of direct evidence by the conclusion of witnesses, or by inspection of the court and jury, *identity may be established circumstantially not only by proving extrinsic facts which render its existence probable, but by proof of indicative manifestations,* such as declarations showing peculiar knowledge, or by conduct, such as residence in a particular country, state, or other place, or service in the army at a certain time. *A family tradition may assist in identification, and hearsay statements in the nature of declarations regarding pedigree are competent for the same purpose.*" (Emphasis ours.)

It is readily seen that the law does not require physical identification of the appellant by his alleged father, who may or may not be able to recognize him in person as they have been separated from each other ever since the appellant was an infant, although in this particular case, the father was able to do so because of having kept in constant touch with his family during all these years and of having received pictures of the appellant from the boy's mother from time to time, one of which was contained in the family group photograph used as an exhibit herein and another attached to the affidavit of relationship. It was therefore arbitrary and unfair for the Immigration officials to disregard this unimpeached, direct, and material testimony given by the appellant's father on the relationship issue. This flagrant disregard of the principles of justice constituted a denial of due process of law.

In the court below, the appellee cited in this connection, the Massachusetts case of *Chung Fong Kwon v. Tillinghast,* 35 Fed. (2d) 398, and *Tillinghast v. Chin King,* 38 Fed. (2d) 5, neither of which has any application to the case at bar. The first one, a District Court case, refers to the failure of the applicant as a native born to produce a birth certificate showing his birth *in this country* where recording of such vital statistics is required by statute. There is no such a requirement in China. The second case refers to the testimony of the identifying witness who has not seen the applicant since he was five and a half years old and not to the testimony of the applicant's father. The identifying witness Gin Wing Fun in the case at bar, testified that he saw the appellant in China in August, 1937 and again in April, 1938 when the appellant was about 12 or 13 years of age [p. 11, Immigration board hearing of July 9, 1940].

IV.

The Appellant Having Satisfied His Burden of Proof by Establishing With Evidence to a Reasonable Certainty That He Was the Son of Gin Ting, the Board of Special Inquiry Was Arbitrary and Unfair in Excluding Him Without Some Substantial Evidence to the Contrary.

The American citizenship of appellant's alleged father Gin Ting was conceded by the board of special inquiry. His trip to China making possible his claim of paternity to the appellant was a matter of official record, San Francisco Immigration File No. 25882/4-4, showing that he departed from the United States on August 22, 1925 and returned from China on May 15th, 1938 when he reported to the Immigration Authorities that he had a son by the appellant's name was born to him and his wife on this trip. Thereafter, on each and every occasion of his several appearances before the Immigration Authorities at San Francisco, San Diego, Tucson and San Pedro, he reiterated the existence of a son by the appellant's name and age. This Honorable Court in *Louie Poy Hok v. Nagle,* 48 Fed. (2d) 753, 755, said:

> "A similar case arose in *Ng Yuk Ming v. Tillinghast,* 28 Fed. (2d) 547, 549 (C.C.A. 1st). There, '13 years before * * * *the alleged father* * * * *testified before the immigration authorities that he has a son bearing the name of the applicant,* * * * *which he confirmed on every other occasion upon which he was called to testify.*' The decision of the Court was that the decision of the immigration officials was not supported by the evidence and the prisoner was ordered released from custody. See, also, Gung You v. Nagle, 34 Fed. (2d) 848 (C.C.A. 9th). In the instant case the cumulative effect of the repeated

> assertions by the father and the previously entered alleged brothers that there was a third son, Loue Fung Leung, born October 1, 1909, certainly go farther than a mere indication that the three were suffering from a delusion; the effect of the testimony in the mind of any reasonable man must be to create the belief that there was a third son somewhere in the offing." (Emphasis ours.)

Other cases holding the same view are: *U. S. ex rel. Lee Kin Toy v. Day,* 45 Fed. (2d) 206; *Johnson v. Ng Ling Fong,* 17 Fed. (2d) 11, 12; *U. S. ex rel. Leong Ding v. Brough,* 22 Fed. (2d) 926, 927; and *U. S. ex rel. Ng Gon Yuen v. Reimer,* 20 Fed. Supp. 976, 977.

The appellant and his father were given a most searching examination by the board of special inquiry at San Pedro. Appellant testified that his name was Gin Soon Ging; that he was born on May 25, 1926 in the Fung Wah Village, Gon Ung Bow section, Hoy-shan district in China; that he had resided in that Chinese village continuously since his birth up to the time of departure for the United States on this trip; that he was destined to his father, Gin Yan Oy, in Los Angeles; that his father's name was Gin Tan (Ting) and Gin Yan Oy was his father's marriage name; that his father was about 60 years of age and a cook by occupation; that his father was married only once, and that was to his mother, Lee Shee; that his mother Lee Shee was 56 years old and her birthday came on the 20th day of the 1st month each year; that his mother was a native of the Nom village, Hoy-shan district in China; that there were three boys in his family including himself; that the oldest boy in the family was Gin Hung Goon, who was about 30 years old and married

to Wong Shee from the Ngor May village in 1933, and they had one son named Gin Thloon Jon born in 1935; that he, the applicant, was the second child in the family; that his younger brother Gin Soon Pang, who was born to his parents in 1927, constituted the third member of his family; that his oldest brother Gin Hung Goon had made two attempts to gain admission into the United States, first time in 1931 and 1937, without any success; that his paternal grandfather was Gin San, or Gin Yat Gim by his marriage name, who died long ago and was buried in the Gai Gung How hill located about a third of a mile north of his home village; that his mother told him his grandfather was married twice—first to Fong Shee of Ung Nan village and after her death to another woman from the same clan and that his father was the son of his grandfather's first wife; that his grandmother and step-grandmother were buried with his grandfather in the aforesaid hill; that as these people died before his birth, he had never seen any of them; that his father had no brothers or sisters; and that his mother was the only child in her family. So much intimate knowledge of the family history the appellant had readily displayed and his alleged father under cross-examination corroborated the same in practically every detail.

As to his native village in China, the appellant testified that he lived in the 4th house on the 2nd row from the head of the Fung Wah village in China all his life up to May 10, 1940 when he left home for the United States; that the Fung Wah village consisted of 12 dwellings, 12 toilets or outhouses, and one school building; that the school-house is on the first row and there were three other rows of houses, each row thereof having four dwellings; that the houses on each row all adjoin each other; that

there was a fishpond in front of the village; that the villagers got their drinking water from a well located at the tail-end of the village close to the fishpond; and that the bamboo hedges at the rear and the two sides and the fishpond in front acted as protective barriers to the village. He made a diagram of the village for the enlightenment of the members of the board of special inquiry and the same was marked Exhibit "B" in the record.

With reference to his ancestral home, the house in which he was born and lived up to the present time, he described as follows:

> "It is a one story green brick house consisting of two bedrooms; two kitchens and one parlor. It has a tile roof and cement floor. There are two outside windows in each bedroom, one above and one below the loft and there are two inside windows between the bedrooms and the parlor. There is one skylight in each bedroom protected by glass and each bedroom has a cross-loft. There is a shrine loft in the parlor, there are two outside entrances, entering into the kitchens."

He further testified that his oldest brother, Gin Hung Goon's family shared this house with them; that his brother Goon occupied the big door side bedroom with his wife and son, while the appellant and his mother and youngest brother Pang slept in the small door side bedroom. His description of the home was used in the cross-examination of his alleged father and no discrepancies thereon could be developed. There could be no question that they shared a very thorough knowledge of the family residence in China.

As to out of ordinary events, the appellant testified that in CR 27 (1938) some bandits attacked his village and kidnapped his mother and oldest brother Gin Hung Goon and that they were later released only upon payment of a ransom. He also told about the unexpected visits by an old friend of his father's by the name of Gin Wing Fun from the United States in 1937 and 1938 bringing money as well as tidings of his father's good health across the ocean. Gin Wing Fun appeared before the board to verify this and identified the appellant as the boy whom his friend and clansman Gin Ting requested him to see when he got to China. Appellee in the court below sought to discredit this testimony because this matter was not contained in a certain questionnaire signed by this witness aboard the incoming steamer upon his return to this country at Seattle in June, 1938. The appellee should be quite familiar with the hasty methods used in filling these form reports when everything is done under pressure and time is very limited for checking and discharging passengers. In the case of *Chan Cheung,* Immigration Bureau No. 55702/44, Inspector Roy M. Porter of Seattle, a man of years of experience in such work, frankly admitted as follows:

> "However, it is known by all experienced officers that the statements taken from incoming Chinese on board the steamers are practically worthless so far as the real truth is concerned, as the *examining officers are hurried in their work and the Chinese persons examined have not the time necessary to think and recall when subjected to such questions in a hurried way. It is well known that nearly every Chinese who departs from the United States takes some letter or money from some friend in the United States to his family in China.*" (Emphasis ours.)

Therefore, it was not without reason for the court to hold in the case of *Flynn v. Tillinghast,* 32 Fed. (2d) 359, that *such alleged answers to a "stock omnibus question" form is a "very slight and insufficient ground on which to adjudge testimony unreliable."*

In reviewing the evidence, there was ample direct and material testimony in support of the relationship claimed by the appellant to his alleged father Gin Ting on the one hand, and not a scintilla of evidence to support the findings of the board of special inquiry to the contrary or to the effect that the appellant was a grandson instead of a son of Gin Ting on the other. Administrative tribunals may ascertain facts in any reasonable and fair manner they see fit, but they cannot reject sworn, consistent and unimpeached testimony without some real reasons which a fair-minded person would regard as adequate; *Ward v. Flynn ex rel. Yee Gim Lung,* 74 Fed. (2d) 145. The burden of proof was so satisfactorily met by the appellant that the board could not cite one material discrepancy between the testimony of the appellant and his father in the hearing. Our courts have repeatedly held that there must be at least some substantial evidence to support an excluding decision; *Nagle v. Wong Ngook Hong* (C.C.A. 9th), 27 Fed. (2d) 650; *Johnson v. Leung Fook Yung,* 16 Fed. (2d) 65; *Johnson v. Ng Ling Fong,* 17 Fed. (2d) 11; and *Leong Ding v. Brough,* 22 Fed. (2d) 926.

Our courts had long ago repudiated the theory that the Immigration Authorities have the power to reject the testimony of any number of apparently credible witnesses

and decide against them in favor of a presumption that an applicant is not an American citizen, but on the contrary, have time and time again restated the rule that *the testimony of one credible witness is sufficient in law to overcome that presumption; Gung You v. Nagle* (C.C.A. 9th), 34 Fed. (2d) 848, 852.

Conclusion.

This case certainly falls under the principle laid down by our Supreme Court in *Tisi v. Todd,* 264 U. S. 131, 44 S. Ct. 260, 63 L. Ed. 590, that the error of an administrative tribunal may be so flagrant as to render the hearing unfair. The uncontradicted evidence established conclusively the relationship of father and son between Gin Ting and the appellant and it was a manifest abuse of power and discretion for the Immigration Authorities to disregard the same without some substantial reason other than the questionable information contained in the anonymous communication. *Go Lun v. Nagle* (C.C.A. 9th), 22 Fed. (2d) 246; *Hom Chung v. Nagle* (C.C.A. 9th), 41 Fed. (2d) 126; *Nagle v. Jin Suey* (C.C.A. 9th), 41 Fed. (2d) 522; and *Gung You v. Nagle* (C.C.A. 9th), 34 Fed. (2d) 848.

It is well-settled that, when a claim of citizenship, which is more than colorable, is denied, the courts will scrutinize the administrative proceedings with great care to the end that American citizens shall not be unjustly deprived of

their citizenship; *Wong Hai Sing v. Nagle* (C.C.A. 9th), 47 Fed. (2d) 1021, 1024; *Woon Sun Seung v. Proctor* (C.C.A. 9th), 99 Fed. (2d) 285. Let us not forget our Supreme Court's admonition in *Kwock Jan Fat v. White,* 252 U. S. 454, 40 S. Ct. 566, 64 L. Ed. 1010, that:

> "It is better that many Chinese immigrants should be improperly admitted than one natural born citizen of the United States should be permanently excluded from his country."

It is therefore respectfully requested that the order of the court below in dismissing the writ be *reversed* with direction to discharge the appellant from the illegal custody of the Immigration Authorities.

Dated at Los Angeles, California, June 23rd, 1941.

Respectfully submitted,

You Chung Hong,
Attorney for Appellant.

No. 9826

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

In the Matter of

GIN SOON GING,

On *Habeas Corpus.*

BRIEF OF APPELLEE.

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No. 9826

IN THE

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GIN SOON GING,

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BRIEF OF APPELLEE.

Statement of the Case.

This is an appeal taken from an order of the District Court denying appellant's petition for a Writ of Habeas Corpus. [Tr. p. 13.] By stipulation and order [Tr. p. 18], certain original immigration and naturalization records have been filed with the clerk of this Court. These files comprise the entire record upon which the administrative finding and order under attack herein was made. Wherever the occasion arises these records will be referred to by their file numbers appearing on the jacket in the righthand corner, excepting the certified Department of Justice file No. 56040/574, which will be referred to as the "Immigration Record". This latter file contains a complete transcript of the hearing accorded Gin Soon Ging by the Board of Special Inquiry.

The appellant, Gin Soon Ging, hereinafter called the "applicant", was born in China and is of the Chinese race. He has never been in the United States. On June 30, 1940, he arrived at San Pedro, California, from China on the SS "President Cleveland" and sought admission to the United States as the foreign-born son of Gin Ting. The United States citizenship of Gin Ting is conceded by the immigration authorities and is not at issue here. The applicant's case was heard by a Board of Special Inquiry appointed under Section 17 of the Immigration Act of February 5, 1917 (8 U. S. C. A. 153). After hearing the testimony offered by the applicant and his witnesses, the Board of Special Inquiry determined the applicant had not established his claimed citizenship status and therefore unanimously voted to exclude him from the United States. From this decision the applicant appealed to the Attorney General. After a hearing by the Board of Immigration Appeals at Washington, D. C., the decision of the Board of Special Inquiry was affirmed and the appeal dismissed. Thereupon the applicant petitioned for a writ of habeas corpus. From an order denying the writ the applicant has appealed to this Court.

The Issue.

This case presents but one issue:

WAS THE APPLICANT ACCORDED A FAIR HEARING?

> "* * * If it does not affirmatively appear that the executive officers have acted in some unlawful or improper way and abused their discretion, their finding upon the question of citizenship must be deemed conclusive and is not subject to review by the court."
>
> *Tang Tun v. Edsell,* 223 U. S. 673, 675.

ARGUMENT.

The rules of law applicable to this case have long been clearly defined. In the case of:

> *Jung Sam v. Haff* (C. C. A. 9, decided December 18, 1940), 116 Fed. (2d) 384,

at page 387, the Court, speaking through Judge Garrecht, stated the principles controlling a review of these proceedings as follows:

> "It is established by a large number of decisions that 'the findings of the immigration officers on questions of fact affecting the right of an alien to enter this country are conclusive against any inquiry by the courts.' Fong Quong Hay v. Nagle, 9 Cir., 17 F. 2d 231, 232. Just as firmly fixed is the rule, in cases of this character, that before this court on review can overturn the determination of immigration authorities it must appear that the evidence submitted on the application for admission so conclusively established the fact in issue that the order of exclusion must be held arbitrary or capricious. Mui Sam Hun v. United States, 9 Cir., 78 F. 2d 612, 615. Denial of fair hearing is not established merely by proving the decision of the immigration officers was wrong. United States *ex rel.* Tisi v. Tod, 264 U. S. 131, 133, 44 S. Ct. 260, 68 L. Ed. 590; Kishan Singh v. Carr, 9 Cir., 88 F. 2d 672, 679. It is of no consequence that this court may have found differently than the immigration officers upon the evidence adduced, for it is not our function to weigh the evidence, but to consider whether or not the applicant was accorded a fair hearing. Mui Sam Hun v. United States, *supra;* Ong Guey Foon v. Blee, 9 Cir., 112 F. 2d 678, 689; Dong Ah Lon v. Proctor, 9 Cir., 110 F. 2d 808, 809, 810."

The applicant seeking admission to the United States has the burden of submitting satisfactory proof of his citizenship.

United States ex rel. Polymeris v. Trudell, 284 U. S. 279;

Quon Quon Poy v. Johnson, 273 U. S. 352;

Mui Sam Hun v. United States (C. C. A. 9), 78 F. (2d) 612;

Won Ying Loon v. Carr (C. C. A. 9), 108 F. (2d) 91, 92.

The applicant in the case at bar has never resided in the United States. He was born in China and is of the Chinese race. Under the treaty, laws and rules governing the admission of Chinese (22 Stat. L. 826; 58, 115, 476, 477:— 28 Stat. L. 7; 32 Stat. L. 176) he is inadmissible unless he can satisfactorily establish that he is a citizen of the United States. He claims he is the legitimate foreign-born son of Gin Ting and that therefore he is a citizen of the United States under Section 1993, Revised Statutes. On this question the applicant, who had the burden of proof, offered no evidence except the oral testimony of himself, his alleged father, Gin Ting, and an unrelated witness, Gin Wing Fun. No documentary evidence of any kind was produced or offered to support the claimed relationship between the applicant and Gin Ting.

It was the duty and function of the immigration authorities to determine if the claimed parent-son relationship actually existed. This question of fact was decided ad-

versely to the applicant by a tribunal authorized by law to consider and decide such a question. Commenting upon this function of the Board of Special Inquiry in the recent case of

> *Young Nguey Sek v. Carmichael* (C. C. A. 9, decided March 11, 1941), 118 F. (2d) 105,

Circuit Judge Denman said:

> "* * * The Board and the Secretary of Labor had to decide no more than that appellant had failed in his burden to show *affirmatively* the parent-son relationship." (Emphasis ours.)

After hearing and weighing the testimony the Board of Special Inquiry, composed of three members, decided the applicant had failed to show affirmatively the parent-son relationship.

This case is a matter of identification involving citizenship. The only evidence presented on this issue was the oral testimony of the interested parties themselves, namely, the applicant and his alleged father, Gin Ting. The testimony of the witness Gin Wing Fun is of no value on this point. He is not related to the applicant and has no personal knowledge of the relationship between the applicant and Gin Ting. He merely testified that he had seen the applicant twice in China, once in 1937 and again in 1938. [Immigration Record, Q. 100-103.] But even in this there is a conflict. Seattle file 7032/2754 shows that when this witness returned from a trip to China June 15, 1938, he was asked under oath if he had visited the home in China

of any resident of the United States or if he had been introduced to the son, wife, or daughter of any resident of this country while in China, and he replied in the negative. When confronted with this contradictory prior testimony the witness attempted to explain this by saying that the interpreter told him it was not necessary to mention what village and who he had visited in China. It was not incumbent upon the Board to accept this explanation and it did not do so.

The testimony of the applicant and that of his alleged father was to the effect that applicant was born in the Fung Wah Village, China, C. R., 15-4-14 (May 25, 1926). [Hearing p. 26 and Immigration Record, Q. 76.] Gin Ting further testified that he had three sons born in China as follows [Q. 76]:

> "1. Gin Hung Guon—age 30, born Jan. 30 or 31, 1912, in Fung Wah Village, China.
>
> 2. Gin Soon Gan (applicant), age 15, born June 24 or 25, 1926, in Fung Wah Village, China, and
>
> 3. Gin Son Pang, age 14, born May 4 or 5, 1927, in Fung Wah Village."

The applicant, likewise, states his alleged father has three sons, as follows [Q. 8]:

> "1. Gin Hing Goon; married marriage name Gin Man Toy, age 30; I never asked my mother when he was born, so I don't know; he was married in our village, C. R. 22-12-20 (Feb. 3, 1933) to Wong Shee of Ngor May Village, Hoy Shan. He was born in our village. He has tried to come to America twice and has been deported twice * * *.

2. Myself.

3. Gin Soon Pang, age 14, born C. R. 16-5-15 (June 14, 1927) at our village and is now home attending the Que Gee School located about one or two li to the South of our village."

It is with respect to the alleged brother-son, Gin Hung Goon, that the most serious discrepancy in the testimony of the applicant and his alleged father appears. File No. 37221/7-27 relates to this alleged brother-son. It shows he twice sought admission to the United States as the son of Gin Ting and was twice rejected. Each time the alleged father Gin Ting appeared and gave testimony. But there were so many discrepancies between his testimony and that of the applicant on family matters and on the question of the age of the applicant that the claim of relationship was rejected. The court's attention is invited to the summary of the Board of Special Inquiry appearing in file 37221/7-27 [pp. 40-45]. The record also shows that a review of that decision was sought in the courts through habeas corpus proceedings but the petition was denied.

The applicant in the instant case now testifies he is the blood brother of Gin Hung Quon, and in so testifying he makes some of the same mistakes his alleged father made regarding this same Chinese. The present applicant identifies a photograph of said Gin Hung Quon as his brother. [Q. 13 and 14.] He testified that said Gin Hung Quon has one son named Gin Thloon Jom, born C. R. 24-6-13 (July 15, 1935) in the Fung Wah Village and that Gin Hung Quon never had any other children. [Q. 10, 11.]

The alleged father, when testifying on behalf of said Gin Hung Quon at San Francisco on August 13, 1937, testified as follows [San Francisco file 37221/7-27, p. 27]:

"Q. How many of your sons have been married? A. My oldest son, Gin Hung Quon.

Q. When, where and to whom was he married? A. I do not know when he was married. He was married in Hong Kong to Wong Shee.

Q. Can you state during what year he was married? A. It was either C. R. 22 or 23 (1933 or 1934). I received a letter from him telling me about it.

Q. Did you keep the letter referred to? A. No, I tore it up.

Q. Has applicant's wife borne him a child or children? A. *He wrote to me in the second letter stating he had a daughter; that is all. It was about a year after he was married that he sent me this second letter.*

Q. Did applicant Gin Hung Quon inform you what the name of his daughter was? A. *Gin Joon Shem.*

Q. Do you know where the wife and daughter of applicant now reside? A. They are now living at the Fung Wah Village." (Emphasis ours.)

And in the same proceeding, Gin Hung Quon himself testified on August 13, 1937, as follows [San Francisco file 37221/7-27, p. 17]:

"Q. How many times have you been married? A. Once only.

Q. When, where, and to whom were you married? A. In C. R. 23-12-12, changes, 23-12-20 (Jan. 24, 1935) to Wong Shee in Fung Wah Village.

Q. Has your wife borne you a child or children? A. No.

Q. Is she an expectant mother? A. I don't know."

Thus we have Gin Hung Quon testifying in 1937 that he had no children, Gin Ting testifying in the same year that Gin Hung Quon had a daughter, Gin Joon Shem, and the applicant in the case at bar testifying that Gin Hung Quon has a son, Gin Thloon Jom, born July 15, 1935.

Speaking of such contradictions in the case of

Won Ying Loon v. Carr, supra,

Circuit Judge Mathews said:

> "Whether in testifying as they did, appellant and Won Doo Mo (alleged father) were deliberately lying or were stating what they honestly believed to be true is, for present purposes, immaterial. Whatever their intentions or beliefs may have been, their testimony was partly, if not wholly, false. Knowing this, and not knowing which part, if any, of their testimony was true, the board was warranted in rejecting it all and holding that appellant's claim that he was Wong Ying Loon had not been established."

The Board of Special Inquiry unquestionably had a right to consider prior departmental records and to base its decision on the discrepancies developed through the use of such records:

Soo Hoo Yen v. Tillinghast (C. C. A. 1), 24 F. (2d) 163;

U. S. ex rel. Ng Kee Wong v. Corsi (C. C. A. 2), 65 F. (2d) 564;

Ex parte Wong Foo Gwong (C. C. A. 9), 50 F. (2d) 360;

Tang Tun v. Edsell, supra.

It is clear, therefore, that testimony of an alleged prior deported brother in conflict with the present applicant may properly be considered by the Board of Special Inquiry and form the basis of an excluding decision. And it has been held that where one applicant's claim is dubious, the claim of the others that he is their brother weakens their assertion:

> *Chung Fong Kwon et al. v. Tillinghast,* 33 F. (2d) 398 (affirmed 35 F. (2d) 1016).

But there is more than this fatal conflict in the testimony of the principal actors in the case at bar. In 1931 Gin Hong Quon, whom the applicant claims is his blood brother, testified that his father, Gin Ting, had been married twice and that he and all the other sons were issue of the second wife, Lee Shee. Both the present applicant and the alleged father have testified that the latter was married once.

Having in mind these contradictions in the testimony, it cannot be fairly said that the Board of Special Inquiry (the triers of the fact) acted capriciously in rejecting the claimed relationship. And, when considering further the fact that there has been no direct identification of the applicant as the son of Gin Ting, it cannot be fairly said that the applicant has sustained the burden of proof. Here the alleged father, Gin Ting, is in no position to identify the applicant as his son. He has not been in China since 1927 when the applicant was slightly over a year old. It is not unreasonable to refuse to accept his testimony under such circumstances. In the case of

Tillinghast v. Flynn ex rel. Chin King, 38 F. (2d) 5,

it was held that where the identifying witness had not seen the applicant since the latter was 5½ years old and the applicant was then 13 years, refusal to accept his testimony was not unreasonable.

Respondent submits that the administrative proceeding in the case at bar was fair in every respect and that there is ample justification for rejecting the applicant's claim.

Reply to Appellant's Brief.

Counsel complains that the Board was arbitrary in refusing to believe the testimony of the applicant because of the discrepancies developed and because the testimony of the applicant and his witnesses agreed in many details.

It is observed that counsel includes in his brief the statement of a certain Inspector Roy M. Porter, of Seattle (p. 15). This particular statement is not a citation from any case but a purported extract from a Department file, which presumably is a part of the Department records at Washington. It is not in evidence or alluded to by administrative officials in the case at bar. It is, of course, recognized that examination of arriving aliens vary in each particular case. This case is like many which involve the citizenship of Chinese applicants. The facts are wholly within the knowledge of interested witnesses, and fabrication can only be detected by the inconsistencies between their versions, or inherent contradictions, since the bare

narration is seldom antecedently improbable. The object of bringing out discrepancies is to impeach the witness or to give a ground for disbelieving him. There is no rule by which the seriousness of discrepancies can be measured. Each case depends upon its own facts.

White v. Chan Wy Sheung (C. C. A. 9), 270 F. 764;

Tom Ung Chai v. Burnett (C. C. A. 9), 25 F. (2d) 574;

Young Mew Song v. United States (C. C. A. 9), 36 F. (2d) 563;

Chan Nom Gee v. United States (C. C. A. 9), 57 F. (2d) 846.

In the case of

Hom Dong Wah v. Weedin, 24 F. (2d) 774,

this court quoted with approval from the opinion in the case of *Sui Say v. Nagle,* 295 F. 676, as follows:

> "In cases of this character, experience has demonstrated that the testimony of the parties in interest as to the mere fact of relationship, cannot be safely accepted or relied upon. Resort is therefore had to collateral facts for corroboration, or the reverse. If the witnesses are in accord as to a number of collateral facts which they should know if the claimed relationship exists, and probably would not know if the claim of relationship did not exist, there is at least a reasonable probability that the testimony is true. If, on the other hand, the witnesses disagree as to the collateral facts which they should or would know if the claimed relationship exists, especially such an important fact as membership in the immediate family of the parties, there is a strong probability that the claimed relationship is false and fraudulent."

Although there are details upon which the testimony agrees, as contended by counsel, it is not possible to reconcile the discrepancies hereinabove commented upon. On this point in the case of

> *Weedin v. Yee Wing Soon* (C. C. A. 9), 48 F. (2d) 36,

Circuit Judge Wilbur said:

> "In the case at bar, we have a multitude of agreements upon a great variety of details in the testimony which are quite consistent with the claimed relationship and point with great emphasis to the truth of the claim. On the other hand, we have a discrepancy that is difficult if not impossible to reconcile with the alleged relationship. * * *"

And, in further comment on this aspect of the case, said:

> "* * * At the outset it must be conceded that there is a complete accord in the testimony upon such a multitude of details as would hardly be expected if the claim of relationship did not exist. Indeed, such a complete accord would hardly be anticipated if the relationship did exist unless there was some previous conference between the witnesses to refresh their memory upon the numerous details upon which they might reasonably expect to be examined."

Counsel also attempts to apply rules of evidence to the proceedings before the Board of Special Inquiry; however, it is not open to the courts to consider either the admissibility or the weight of proof according to the ordinary rules of evidence, and the fact that the rules of evi-

dence as applied in courts of law are violated does not show that the hearing was unfair.

Healey v. Backus, 221 Fed. 358;

Frick v. Lewis, 195 Fed. 693;

Lee Lung v. Patterson, 186 U. S. 168, 176.

Appellee submits that the discrepancies developed in this case are sufficiently serious to preclude the determination that the applicant was not given a fair hearing or that the District Court erred in sustaining such finding. The record fully bears out District Judge Beaumont in his conclusion [Tr. p. 14] that:

> "After a study of the record herein the Court cannot say that the Board of Special Inquiry committed a manifest abuse of the power and discretion conferred upon it. In this case the evidence is such that reasonable men might differ as to its probative effect."

Conclusion.

For the reasons hereinabove stated, appellee respectfully submits that the lower court did not err in holding and finding that there was no manifest abuse of discretion by the immigration authorities, and that the administrative order was not a result of an arbitrary or unfair hearing. Wherefore, appellee prays that the decision of the lower court be affirmed and appeal dismissed.

Respectfully submitted,

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